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OUTER CONTINENTAL SHELF REVENUES

HEARING

BEFORE THE

COMMITTEE ON ENERGY AND NATURAL RESOURCES UNITED STATES SENATE

NINETY-NINTH CONGRESS

FIRST SESSION

ON THE

DISTRIBUTION OF OUTER CONTINENTAL SHELF SECTION 8(g) REVENUES IN RESPONSE TO INSTRUCTIONS FROM THE BUDGET RESOLUTION

SEPTEMBER 24, 1985

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OUTER CONTINENTAL SHELF REVENUES

TUESDAY, SEPTEMBER 24, 1985

U.S SENATE,
COMMITTEE ON ENERGY AND NATURAL RESOURCES,
Washington, DC.

The committee met, pursuant to notice, at 9:05 a.m., in room SD-366, Dirksen Senate Office Building, Hon. James A. McClure, chairman, presiding.

Present: Senators McClure, Domenici, Wallop, Warner, Murkowski, Nickles, Hecht, Evans, Johnston, Bumpers, and Metzenbaum.

Also present: Gary G. Ellsworth, chief counsel; and James T. Bruce, counsel for the minority.

OPENING STATEMENT OF HON. JAMES A. McCLURE, A U.S. SENATOR FROM THE STATE OF IDAHO

The CHAIRMAN. Good morning. This is an oversight hearing of the full Committee on Energy and Natural Resources to receive testimony concerning the distribution of section 8(g) Outer Continental Shelf leasing revenues in response to instructions from the budget resolution.

While those instructions did not mandate that this committee resolve the longstanding difficulties associated with the distribution of section 8(g) revenues, it is nevertheless clear to the chairman, as well as other members of this committee, that resolving this matter is necessary in order to achieve the savings in the budget resolution that this committee is mandated to achieve.

The question before us this morning, then, is not if the 8(g) issue will be resolved, but rather how it will be resolved. Assisting the committee this morning in sorting through this extremely complex matter will be the Secretary of the Interior, Don Hodel, and the Governor of the State of Texas, Hon. Mark White.

Gentlemen, I want to welcome and thank you both for appearing here this morning, especially on such short notice. I know how strongly you both feel on this important issue, and we look forward to your testimony.

I would note that we are under very severe time constraints this morning. Besides Senators having other important committee meetings, Secretary Hodel must leave by 10:30 a.m. in order to catch a plane. I would, therefore, ask other Senators to include their full statements in the record and keep any necessary oral statements brief.

I would also note the committee is scheduled to continue its markup of actions pursuant to the budget resolution this afternoon at 3 p.m., as we must report to the Budget Committee by this

Friday. It is my sincere hope we can resolve all matters before the committee before sundown this evening.

Mr. Secretary, would you please come forward. We will get to your testimony as quickly as possible. Let me express my thanks to you for being able to respond as quickly as you did. I realize that it was not easy. I know you had to make adjustments in your schedule to do so, but we do appreciate it.

Senator METZENBAUM. Mr. Chairman, may I say one word?

The CHAIRMAN. Yes.

Senator METZENBAUM. As you know, I was very anxious for the Secretary to appear before the committee, and I am very pleased he is here. I just want to explain to both you and him that, due to a previous commitment, at 9:30 for a short period of time I must walk out. I don't want him to consider that an insult nor indicate to you a lack of interest. I will be back.

The CHAIRMAN. Thank you.

Mr. Secretary.

STATEMENT OF HON. DONALD PAUL HODEL, SECRETARY OF THE INTERIOR

Secretary HODEL. I would like to submit, if I may, my prepared statement for the record and briefly summarize what I think the issue is.

The CHAIRMAN. Your prepared statement will be placed in the record in full.

Secretary HODEL. I very much appreciate the opportunity to have this hearing today. I know that there was a possibility that we would not.

I recognize the authority of the Congress and this committee to do anything in this area it chooses to do. It is even possible that the proposal before this committee would help me on another issue which is of national significance, the moratorium issue which will be confronting committees of this Congress. It might engender some additional support among some of the key States for the OCS Program.

But I could not, in good conscience, let this go by without at least trying to have an opportunity to explain to this committee what I think is at stake here in terms of the dollars involved—what is basically here, I believe, is a significant amount of unjustified largesse to mostly three States out of the Outer Continental Shelf account.

The amount of money involved today substantially exceeds the amounts of money I am usually arguing about over the budget of the Department of the Interior. If I could have the amount at stake to play with, I could come before this committee and other committees of the Congress and solve everybody's problems. It is a very significant amount of money.

With your permission, Mr. Chairman, I would like to illustrate this point using a flip chart. The maximum amount of money that has previously been suggested—and I will get to what the account is in due course, but I think the essence of this issue can be explained in these terms—the most geologists have suggested should go to the States out of this account is somewhere between 1 and 4

percent. In fact, our experience suggests it is something more toward the 1- or 2-percent range which would, in fact, be appropriate.

Last year Secretary Clark, in an effort to resolve this matter, suggested and obtained administration approval for a proposal that 16⅔ percent of the rents and bonuses in the 8(g) account, which I will talk about, plus the interest on them be paid to these States.

When I became Secretary in February, I renewed this offer to the States. They had initially rejected it. I renewed the offer, and the States responded by saying they wanted 37½ percent, not only of rents and bonuses, but also they wanted royalties and taxes, Federal taxes included. That would be a very sizable difference in the pot.

In May of this year, the House Budget Committee approved a concurrent resolution which said that 27 percent of the rents and bonuses then in escrow should be distributed to the States.

I will get a little ahead of my story and go to the conclusion, if I may. What is at stake today is whether that account will be expanded to include royalties and possibly taxes, because there is language in the proposal before this committee which clearly raises the issue about taxes. The effect would be a known, immediate, subject to the availability of funds, payout of $6 million from the Federal Treasury, and over the next 30 years, we estimate anywhere between $6 and $12 billion additional which will go primarily to Texas, Louisiana, and California.

And, instead of resolving the litigation, which was the intention of this settlement effort, the Justice Department has agreed with us that the language in the resolution will almost assuredly lead to litigation over the calculation of taxes and the amount of taxes which in the future would be required.

Now, that in essence is the problem for the committee and I would like to explain a couple of the key points that get us there. The first has to do with the 8(g) zone. Is this [indicating] visible to all of the members?

The blue area on this chart represents State onshore and offshore areas. As you know, some States go out 3 miles and some States go out 3 leagues. But there's eventually a line which is a boundary between State and Federal waters. The 1978 OCS Lands Act provides that, in section 8(g), the next 3 miles of that zone is an area from which drainage the Federal Government says is to be paid on a fair and equitable basis to the States.

There's been some dispute, Mr. Chairman, over whether or not "fair and equitable" was intended to apply to drainage. I think it's a matter which is almost without dispute if we look at the legislative history. And I may say, this would be more relevant in court than it would be before this committee because, if this committee and Congress decide to change the rules, you certainly are privileged to do so, but at enormous cost to the taxpayers.

In March 1977, Congressman George Miller from California pointed out that he believed that a section 8(g) would be necessary because, he said, current law permits a Federal lessee—that is, someone leasing from us in these [indicating] waters—to capture a State's resources without adequate compensation. The only result of section 8(g), he said, would be that "The State-owned subsurface

resources would accrue to the State regardless of how they were produced, which seems fair."

Secretary Andrus, in response to that, in May 1977, sent a bill to the Congress in which he explained the purpose of 8(g) and he said: "We favor a provision which gives coastal States fair and equitable compensation for oil and gas which is produced through wells on Federal waters adjacent to them, but which is derived from State lands."

That is what we normally mean by drainage: oil and gas derived from State lands. That is what gave rise to that 1- to 4-percent calculation, because when the geologists look at the real world there's a very limited amount of actual drainage taking place.

Now, let me just point out some of the situations we have gotten into with these tracts. This is again a 3-mile zone. The blue line represents the outer limit, while white is the Federal area. If we take example A, we have a tract which is entirely within the 3-mile zone, and that tract, for instance, if it drew a $44 million bid and had the common pool, under our proposal $11.9 million—27 percent of the $44 million—would go to this State.

That is what would occur under the committee proposal. There would be no difference on a tract entirely within the 8(g) zone, but there is where we begin to diverge and where a great deal of money becomes involved.

The next example is tract B, which has 95 percent of the tract within the 8(g) zone, 5 percent outside. We would prorate. We would say that on a $17 million bonus that $4.3 million would go into the 8(g) account. Under the proposal before the committee, $4.6 million would go into the account because all of the proceeds would go into the account regardless of the fact that part is outside. It gets worse, however.

We move up to C, which is 12 percent inside the zone, $35 million. We would put $1.1 million in the account. But under the committee proposal, $9.5 million would go into the account although as we can see 88 percent of that tract is not even remotely in the 8(g) zone and there is no pool which overlaps into State waters. The State would be receiving not only the benefits of this small portion, although there is no connection to the State, but it would be receiving the portion outside.

The most egregious example—and by the way, these are taken from actual examples on the OCS Program, as you might have guessed—$36 million in tract D was the bid and 0.1 percent of the tract is in the 8(g) zone. If we do not pro rate the $36 million bid for this tract, we would place $9,000 in the account.

The CHAIRMAN. How much?

Secretary HODEL. $9,000. And the committee's proposal would put $9.7 million on the account, a very significant difference.

Let me move from that, then, and suggest that in the building of this account there is one more item we need to review—the present status of the account. This [indicating] is rents and bonuses, including a small amount of royalties. As of March 31 of this year the account was $5.8 billion.

If we had been consistent in prorating as we now propose to be, that account would be $5.1 billion. There is about $700 million in

the account which is a result of our not prorating because of some court orders.

If we take the proposal before the committee, we will expand this to include royalties and taxes, and our estimate is that the cost over time will be between $6 and $12 billion. And that is, as I say, the essential issue before the committee, whether the account to which the 27 percent should apply is smaller or larger.

If you multiplied this account [indicating] by 27 percent, you come up with our $6 to $12 billion figure.

Now, Mr. Chairman, I think the correspondence and the language of the act make it fairly clear that it really isn't a close question. I admire very much my friends from Louisiana and Texas with whom I have dealt on many OCS issues and on which we are normally allies.

I have the highest respect for them, and it seems to me they are, in the finest tradition representatives of their States, obtaining potentially an enormous windfall for their States. They are persuasive. They are representing their constituents.

But it seems to me incumbent upon the administration and the Congress, representing the rest of the country and the Treasury of the United States, not to permit this kind of change and distortion in the program to take place.

Mr. Chairman, with that I would be happy to submit myself to questions.

[The prepared statement of Secretary Hodel follows:]

Testimony of Donald Paul Hodel
Secretary of the Interior
before the
Senate Committee on Energy and Natural Resources
September 24, 1985

INTRODUCTION

Mr. Chairman and Members of the Committee, I appreciate the opportunity to appear before you today to present the Administration's views on legislation to settle the issues surrounding Section 8(g) of the Outer Continental Shelf (OCS) Lands Act. This is a very complex matter involving the proper distribution of billions of dollars in federal OCS revenue between certain coastal states and the federal government. It has major budgetary implications and thus is a matter of great concern to this Administration and to all Americans concerned about the fiscal integrity of this Nation.

As you know, Section 8(g) was enacted as part of the 1978 amendments to the OCS Lands Act. It established certain leasing policies regarding the first three miles of the federal OCS, abutting state submerged lands. More specifically, Section 8(g) provided for the "fair and equitable" sharing of those revenues produced from federal leases in this three mile zone from oil and gas pools common to both federal and state submerged lands.

It established a framework for the federal and coastal state governments to agree to the terms of a distribution of federal revenues. Failing such an agreement, revenues from the 8(g) zone were to be deposited in a separate interest-bearing account. Since 1978, this account has grown to over $6 billion.

We share a common goal today to resolve these longstanding 8(g) disputes in a manner which fairly distributes the current account between seven coastal

states and the federal government. We also seek a future arrangement which avoids costly and unnecessary litigation over this issue and strikes a reasonable balance in the future sharing of 8(g) revenues.

The Administration has proposed legislation which accomplishes both of these important goals. I would like to discuss the elements of that proposal today and explain why it is abundantly fair to the claims of affected coastal states. I also would like to explain the basis for our strong opposition to the counterproposal before this Committee in the form of a markup vehicle. It is, in our opinion, the worst of all possible approaches.

It not only constitutes a huge giveaway of federal revenue, far beyond the original intent of Section 8(g), but it ensures that litigation over federal leasing will continue well into the future. In this regard, it fails to achieve either of our principal goals.

It should also be recognized that the proposed payout to the seven coastal states will come from the federal Treasury. From a budget perspective, since this money has never been counted as a receipt, this money can be "scored" when the 8(g) issue is settled. But that does not really reduce the federal deficit. In fact, the Treasury will have to borrow an additional $1.4-$1.6 billion to comply with the proposed legislation.

BACKGROUND

Critical to any resolution of the current controversy is an understanding of the context and intent of Section 8(g). Congress had a specific problem in mind, i.e. drainage. Its solution, in the form of 8(g), was meant to avoid federal/state conflicts over OCS leasing, not to create them.

The roots of this issue extend to the beginning of this century when oil was discovered in the seabeds off our coasts. This discovery gave rise to conflicting claims of ownership by the federal and coastal state governments. Litigation ensued. In a series of opinions beginning in 1947, the Supreme Court ruled that the federal government, rather than the states, had paramount rights in, and power over, all offshore seas and submerged lands, including all offshore mineral resources.

The coastal states carried their cause into the political arena. In 1953, Congress enacted the Submerged Lands Act, granting to such States full rights and ownership in the first three miles (or, in the case of Texas and the Gulf coast of Florida, leagues) of offshore waters and seabed. These states have since developed the resources contained in these waters, benefiting by billions of dollars in offshore revenue. This same Act, and its companion legislation, the OCS Lands Act, confirmed the federal government's jurisdiction over and right to the OCS and the minerals.

The OCS Lands Act remained essentially untouched until 1978 when Congress enacted the OCS Lands Act Amendments designed to achieve two vital national objectives: expeditious development of the entire OCS and environmental protection.

Section 8(g) was a side issue in this equation.[1/] It was added to the House version of these amendments to help resolve state concerns--first raised by California in 1975[2/]--about possible drainage of state resources. Since oil and gas migrate underground, state resources can be produced from wells in federal submerged lands.

The basis of these concerns was the common law rule of capture which applied to oil and gas production. Under this rule, a common pool of oil or gas underlying both state and federal submerged lands would belong to whoever first produces it from either side of the jurisdictional line. If the federal government were to develop OCS resources adjacent to state submerged lands, adjacent states would be faced with potential drainage of common oil and gas pools underlying state submerged lands. While those states could drill offset wells (wells to extract oil and gas from state submerged lands) to federal leases to protect their right to pursue the resource, this would lead to an inefficient doubling of the amount of drilling activity. In addition, California had legislated a prohibition on leasing in certain coastal areas and had no desire to lease for offset purposes in these areas.

1/ Congressional Research Service, 1984, "Fair and Equitable Disposition of Common Pool Revenues under Section 8(g) of the Outer Continental Shelf Lands Act," p. 2.

2/ As early as 1972, Governor Edwards of Louisiana complained to the Congress that there was no "mechanism" in the law to protect Louisiana from drainage of oil and gas in common reservoirs by federal leases.

(Hearings before the House Committee on Interior and Insular Affairs, 92d Cong., 2d Sess., Appx. 1390 (1972)).

The push for such a provision came in 1975 when the California State Lands Commission testified about its concern that federal lessees could drain oil and gas from common reservoirs partly underlying California's offshore oil and gas sanctuaries.

(Hearings before the House Ad Hoc Select Committee on Outer Continental Shelf, 94th Cong., 1st Sess., 1388 (1976)).

To solve this dilemma, Congress chose to share revenues with coastal states from such common oil and gas pools, so that states would not be compelled to drill just to protect themselves from drainage. This intent of Section 8(g) was abundantly clear from the Conference Report to the 1978 Act, which explained that:

> "While the issue of jurisdiction over offshore lands has been resolved by the United States Supreme Court in United States v. Maine, 420 U.S. 515, 95 S. Ct. 1155 (1975), the problem of drainage of State resources by a lessee operating on the Outer Continental Shelf has not been so resolved." H.R. Rep. 94-1084, 94th Cong., 2d Sess., p. 95 (1976)

Appreciation of this "drainage only" intent of Section 8(g) is critical to determining an appropriate sharing of 8(g) revenues. This is particularly important since little or no drainage from state waters actually occurs. To date, on 8(g) leases, the only drainage that has actually occurred has been by Texas of federal resources in the Sabine Pass area. Estimates of the value of future drainage range from 1-4 percent of 8(g) lease revenues, although we believe it probably does not exceed 2 percent and that amount may be offset by State drainage of federal resources. To put it into context, it appears distribution of all 8(g) revenues on the basis of drainage could result in no payment to coastal states from the current 8(g) account and approximately $100 million over the life of the federal 8(g) leases. This compares with our proposal of $1.4 billion to coastal states from the current account and hundreds of millions of dollars in the future. The right to an even greater distribution of federal revenues is neither justified nor fair to the interests of the Nation as a whole.

REVENUE COMPONENTS OF SECTION 8(g)

It is important to distinguish the various revenue items which accrue to the federal government owing to the economic value of the underlying resource in the Section 8(g) zone. The predominant bidding system applied in the 8(g) zone provides for bonus bidding with a 16 2/3 percent royalty. Royalties are assessed on gross production value absent consideration of costs.

If companies assume that tracts adjacent to federal 8(g) tracts will be leased (or if they are leased), then bonus bids will only reflect value expected from the resources underlying that tract and not resources underlying adjacent tracts. State regulatory agencies have the authority (as does the Minerals Management Service (MMS)) to direct their lessees to prevent the capture of State resources by adjacent federal lessees.3/

Even though bonuses in the 8(g) zone likely reflect resource value only from those areas and not state resources, theories have been advanced which argue that bonus bids are higher on federal tracts because of prior drilling on state tracts. It has been alleged that state leasing has "enhanced" federal bonuses in the 8(g) zone. While the federal government disagreed that this "bonus enhancement" theory is compensable under Section 8(g), the Administration has agreed to some sharing of bonuses as a means to resolve this 7-year conflict.

3/ The Minerals Management Service did direct federal lessees to drill additional wells in the Sabine Pass areas to prevent drainage of federal resources by state lessees.

States have also argued for general royalty sharing, but their rationale has been simply an "equities" theory, which the courts have not accepted. There has been no counterpart to the "bonus enhancement" concept for royalties, and the Department knows of no basis for sharing royalties on a flat percentage basis. If situations arise where drainage of state resources may occur, we have proposed unitization or royalty sharing agreements as a means for compensating states for this value. Any sharing of royalties above this drainage potential represents an unjustified redistribution of public resources to a select group of coastal states.

THE ADMINISTRATION PROPOSAL

The Administration has given this Committee language that would pay to the states approximately $1.4 billion in Fiscal Year (FY) 1986 from the current account representing 27 percent of bonuses, rents, and accrued interest from 8(g) tracts without regard to common pools. This is consistent with the recommendations that accompanied the Budget Resolution which assume "that the legislation will settle the dispute and give the States a 27 percent share of the bonuses and rents in escrow as well as the interest that has accrued on them."

The Administration proposal goes beyond the recommendations by amending Section 8(g) to provide states with 27 percent of future bonuses and rents attributable to the 8(g) zone. Royalties, since they are not received until

the well is produced, and thus when geological data is available to determine if a common pool exists, would be paid on the basis of actual drainage.[4/] The cost to the federal government of this royalty payment based on actual drainage is estimated to be approximately $100 million over the life of the Federal leases.

In addition, all claims arising under the current Section 8(g) would be extinguished and 50 percent of all bonuses and rents received by a state would be passed through to elected local governments of affected coastal states. This is a significant concession by the federal government on the amount of money required by Section 8(g) to be paid to coastal states from federal oil and gas resources.

MARKUP VEHICLE

The markup vehicle would pay to states approximately $1.6 billion in FY 1986 from the current account, $200 million more than the Administration's proposal. In addition, the "recoupment" section of the markup vehicle asserts that there are revenues that "should have been" deposited into the current account and were not and, therefore, the states are entitled to an additional $600 million over the Administration's proposed $1.4 billion payout. The main basis for this assertion is the issue of prorationing the bonus by surface acreage.

4/ Federal and state experts would determine the amount of oil and gas from a reservoir originally in state or federal submerged lands and allocate the production accordingly.

(1) Prorationing by Surface Acreage

Section 8(g) does not provide for the payment of money to states from revenues generated beyond the 8(g) zone. The statute is clear in talking about revenues only from areas, not tracts, within three miles of the seaward boundary of a state (and then only if there are common pools or fields with state submerged lands). Many of the blocks previously leased contain acreage that extends beyond the zone further into the federal seabed of the OCS.

As an example, the one tract leased offshore Florida is only partly within the 8(g) zone. Of the 5,760 acres included in the leased block, only 477 acres (about 8 percent) are within the three mile 8(g) zone. The largest bonus ever received for any tract leased on the OCS was $334 million in Sale 53 offshore California. Only 40 percent of that tract lies within the 8(g) zone. Offshore Texas, there is a tract with only 17 acres out of 5,760 that lie within the 8(g) zone, amounting to .2 percent of the tract. Similarly, offshore Louisiana, there is a tract where only 82 acres of a 2,497 acre tract lie within the zone, amounting to 3 percent of the tract.

There are many more examples of this type. The markup vehicle would require the federal government to share 100 percent of the bonus, rent, and royalties from these overlapping tracts, no matter how small the percentage of the acreage in the tract is within the 8(g) zone. In effect, this is equivalent to an assumption that 100 percent of the tract's resources are within that portion of the Section 8(g) zone.

We believe it is unconscionable and overreaching to ask the federal government to share 100 percent of the revenues from such tracts when only a part of the acreage falls within the 8(g) zone. Although it is true that the District Court for the Eastern District of Texas enjoined the Department from prorating bonuses from tracts overlapping the 8(g) zone for revenues deposited in the 8(g) account, that was not a ruling on the merits of proration. It was merely an interim means to protect the court's jurisdiction on this issue.

When the Court did rule in 1984 on this question, Judge Parker concluded that "Some tracts are not entirely within the 8(g) zone. To the extent these tracts extend beyond the 8(g) zone they are beyond this Court's jurisdiction in the sense that this Court cannot distribute federal revenue attributable to non-8(g) lands." State of Texas v. Secretary of the Interior, 580 F. Supp. 1197, 1204 fn. 41 (E.D. Tx 1984). Although he did require the Secretary to deposit all revenues attributable to overlapping tracts to the account, he only did so because he wanted the funds available in the unlikely event that he would find that the value of the entire tract was derived from a common pool underlying both the state submerged lands and the federal submerged lands within the 8(g) zone. We believe that, based on the geology of the 8(g) zone, such a finding would be very rare. Of the nine tracts for which Judge Parker awarded money to Texas, only one had acreage which extended beyond the 8(g) zone--and only 7 percent of that tract was beyond the 8(g) zone.

(2) Future Payments from the 8(g) Zone

For purposes of future 8(g) revenues, the markup vehicle amends Section 8(g) to provide states with 27 percent of bonuses, rents, royalties, and other revenues from federal leases in the 8(g) zone. While the Administration

supports amending Section 8(g) to provide states with 27 percent of bonuses and rents, we strongly oppose any amendment to Section 8(g) which would provide states with 27 percent of royalties and "other revenues."

Royalties

We estimate that inclusion of a 27 percent distribution of royalties to the states will cost over $4 billion over the next 30 years. While it is true that there is only about $200 million dollars in royalties currently in the 8(g) account, the leases in question were issued no more than 6 years ago. Most of them were issued within the last 3 years. It generally takes between 5-15 years for production to begin from offshore leases. It is only natural that there would not be very much royalty revenue from leases that are in their early stage of development.

From leases offshore California in the 8(g) zone, there are essentially no royalty revenues in the 8(g) account. That is because there has been essentially no production from those leases. However, from known discoveries, there are 550 million barrels of oil and 700 billion cubic feet of gas expected to be produced from those leases between now and the year 2015. At $25 per barrel for oil, that is $17.5 billion dollars for the value of the production, of which the federal Treasury would receive over $3 billion in royalties. With only moderate price increases over the 30 years during which it is expected that this oil and gas would be produced, the royalty value would be in excess of $4 billion. That means for California alone, the expected additional payment by including royalties at 27 percent would be in excess of $1 billion. We anticipate other discoveries from existing leases in the 8(g) zone offshore California that would increase this number even more.

The MMS has not developed reserve estimates for known discoveries in the 8(g) zone offshore other States, but a recent study, using actual production and known reserves in the Gulf of Mexico, estimates that the value of royalties collected by the federal government will be in excess of 2.5 times the bonus received for tracts leases. We could anticipate an additional $3 billion in payments to Gulf states from royalties from 8(g) tracts. This does not even include figures for Alaska. The estimate of an additional payment of $4-6 billion, therefore, has a firm foundation.

"Other Revenues"

The Committee markup vehicle requires that 27 percent of "other revenues" from federal leases on the 8(g) zone be distributed to the states. The states have argued in the ongoing litigation that the term "other revenues" in the current law includes federal taxes, including windfall profit taxes. We believe that now that we have agreed to share all bonuses and rents received from the zone without regard to common pools--a major concession beyond what is required by the current law--the requirement to distribute a share of "other revenues" should not be included in the statute. Including the term will only guarantee future litigation over this issue. This phrase could result in further unjustified payments to a few states at the expense of the general public. We have not been able to prepare a precise estimate, but our economists speculate it could cost between $1-5 billion.

(3) Extinguishment of Claims

The Administration believes that one of the major purposes of any legislation should be to resolve all continuing disputes with coastal states over the proper distribution of revenues from the 8(g) zone. If the United States is compelled to continue any litigation on this issue, there is no

benefit to the United States in enacting any settlement legislation since we believe that we would do better in court on behalf of the general taxpayer than provided in the proposed markup vehicle. We support language that would repeal Section 8(g) and extinguish all rights under it. In lieu of those rights, the states would receive payment from the current fund.

The markup vehicle, leaves Congress' intentions unclear. Section 533(c) appears to leave a state with the option of accepting payment under the bill or continuing litigation under the repealed provisions of Section 8(g). Such an implication is unacceptable, promising more years of litigation.

(4) Information Sharing

The state rightfully should have access to geologic and geophysical information from the three mile 8(g) strip. We fail to see the need, however, for the enormously broad information sharing requirements in the proposed markup vehicle. Section 532 of the proposed markup vehicle states that the Secretary shall provide the Governor:

> "all information from all sources concerning the geographical, geological, and ecological characteristics of such regions; an identification of any potential hydrocarbon-bearing area or areas located wholly or partially within three nautical miles of the seaward boundary of such coastal state, including all information relating to the entire potentially hydrocarbon-bearing area."

I am sure that some states could and would read this as a requirement to give them at no cost all information in the possession of the MMS (and if taken literally, all information available about such regions--whether in the hands of the MMS or not) bearing on the whole OCS. Protection of proprietary information is a serious responsibility of the Department which affects incentives to gather such data. We fail to understand the necessity for states to receive this material from the entire OCS. Duplicating costs alone could be enormous. Increasing the distribution of this information increases the risk of release, and such release may seriously harm the incentives for private contractors and lessees to gather geophysical information and conduct other types of exploration activities. We therefore conclude this provision is unnecessary and unreasonable.

(5) Interest Rate Provision

We are also concerned about the requirement in the markup vehicle that money held in interest-bearing accounts in the Treasury must be invested to yield "the highest available interest rate." This provision will also undoubtedly lead to litigation over whether the "highest available interest rate" was obtained.

Money deposited into interest-bearing accounts in the Treasury ordinarily bears interest at rates taking into consideration current market yields on outstanding marketable obligations of the United States. However, this language could require high-risk investments that would not be in the overall best interest of the account.

(6) Alaska Section 8(g) Agreement

In 1979 the first offshore lease sale was held in the Beaufort Sea. That sale was a joint federal/state lease sale. For that sale, the DOI and the state of Alaska signed an agreement pursuant to Section 7 of the OCS Lands Act to provide for leasing of disputed acreage.

A Section 8(g) agreement was also signed by the state of Alaska and the DOI to cover the eventual distribution of the revenues from the 8(g) zone. Alaska agreed to accept payment for revenues from the 8(g) zone based on drainage of the resources from state lands. There is a provision in the markup vehicle invalidating that agreement and, instead, treating this sale like those for which there has been no agreement. This action has a potential cost of $250 million. We object to this provision because the state and the Secretary of the Interior have already reached a "fair and equitable" agreement concerning the distribution of the revenues from that lease sale.

(7) Duplicative Sharing of Production Revenues

In addition to the unacceptable sharing of 27 percent of royalty revenues, the markup vehicle requires the Secretary to share even more "revenues from production of any potentially common hydrocarbon-bearing area." This language fails to give any criteria on how the Secretary and a Governor are to agree on the division. While it appears to be protection against drainage, it is not expressly so limited, and leaves open the possibliity that states will argue for a share of federal taxes. Additionally, it uses the phrase "hydrocarbon-bearing area," which has no accepted meaning among petroleum geologists, and contains no procedure for resolving the inevitable disputes this language will create. While the goal of protecting the states against drainage is sound, this provision is an unworthy attempt to serve that goal.

(8) Distribution of Leasing, Exploration, and Production

Section 8(g) is a dispute between state and federal governments over money. There is no reason why a court should be able to enjoin OCS leasing, exploration, development, and production because of this dispute. Yet the markup vehicle repeals that existing anti-injunction provision in the current law. Consequently, this bill promises to interfere with the opportunities of private companies to find and supply the oil and gas this Nation needs, and could provide the opportunity to bring the OCS leasing program to a sudden halt.

ONSHORE REVENUES VERSUS OFFSHORE REVENUES

An argument that frequently arises is comparison of the 8(g) issue with the sharing of revenues from onshore mineral leasing activities. However, such a comparison overlooks several critical distinctions. First and foremost, unlike production on the OCS, onshore leasing activities actually occur within state boundaries. Therefore, there is a greater potential for federal onshore leasing activities to affect certain state perogatives, such as the right to free use of the surface estate, where the federal government only holds rights to the minerals.

Moreover, the Mineral Leasing Act of 1920 was always intended as a general revenue sharing measure. It was meant to provide funds to states because of their inability to tax federal lands within their borders. Since the 8(g) areas are outside state borders--in fact three miles beyond state land--no similar loss of tax revenue occurs. Section 8(g) was never designed as a general revenue sharing provision, but was included in the OCS Lands Act Amendments of 1978 to address the particular problem of drainage. In summary,

the analogy of onshore revenue sharing simply does not fit. This is federal leasing of federal resources totally outside any state territory.

CONCLUSION

In conclusion, I want to emphasize that the Administration wishes to resolve the issues surrounding Section 8(g). We cannot support legislation, however, which will place massive new demands on the revenues of the federal Treasury and which will not eliminate the litigation arising from Section 8(g). We support a 27 percent share of bonuses and rents to be paid to the states, but only if the bonus is prorated by the percent of the acreage actually within the three mile 8(g) zone. We also support the payment of royalties to states based on drainage only.

It is estimated that the markup vehicle would cost the Treasury from $6-$12 billion more than the Administration's proposal. These added costs constitute an unjustifiable diversion of revenues belonging to all taxpayers to the benefit of a select few. There is simply no basis for these outlays.

This concludes my prepared testimony. I would be pleased to answer any questions which Members may have.

The CHAIRMAN. Thank you very much.

Senator Johnston.

Senator JOHNSTON. Thank you, Mr. Chairman.

Thank you very much, Secretary Hodel, for your kind words. I would also say that, given the very short period of time that you have had to prepare for this, you have done very well, although I must say that the facts which you relate contain a breathtaking, not to say astonishing, lack of presence.

Let me start off with the fact that you say geologists all say the States' share should be 1 to 4 percent of this. Of course, the problem is that that assumes that this legislation concerns only drainage, isn't that correct?

Secretary HODEL. Yes.

Senator JOHNSTON. And the problem is the court has specifically ruled that it involves more than drainage. If you haven't had a chance to read the court's decision, let me read it. And this is the only case on the subject. I could read it at length, but just let me give you a full paragraph from State of Texas versus Secretary of the Interior, 580 Federal Supp. 1197, page 1199:

> After thoroughly reviewing the parties' motions and supporting briefs, the voluminous legislative history, the statute, and after nine days of trial, the court has concluded that disposition of Federal lease revenue pursuant to section 8(g)(4) is not limited to compensation for drainage. Accordingly, the plaintiff's motion to reconsider is granted.

Senator METZENBAUM. The word is what, is not what?

Senator JOHNSTON. "Is not limited to drainage."

Senator METZENBAUM. All right, thank you.

Secretary HODEL. May I respond? You don't want me to respond yet?

Senator JOHNSTON. Let me go on just a minute.

And you said in your letter:

> Some tracts are not entirely within the 8(g) zone. To the extent that these tracts extend beyond the 8(g) zone, they are beyond this court's jurisdiction, in the sense that this court cannot distribute Federal revenues attributable to non-8(g) land.

That's your letter. Unfortunately, you left out the next two sentences, which say: "The court has taken this factor into consideration in formulating a fair and equitable division of revenues attributable to tracts part within and part without the 8(g) zone. For future lease sales involving such tracts, the Secretary should deposit in the escrow account all revenue attributable to such tracts, because in the absence of an agreement between the Secretary and the Governor, the determination of what percentage of revenue is attributable to the 8(g) portion of a particular tract is a finding of fact, appropriately made by the court."

Now, what you are saying is in effect, if we disregard the law and you use 1 to 4 percent, then you are right. But wouldn't you agree with me, if you follow the law, at least the law as stated by Judge Parker, those figures are preposterously wrong?

Secretary HODEL. Well, I would respectfully disagree from this standpoint. The court did not deal with royalties. It specifically did not deal with the issue of royalties, which is a very significant share of this.

Senator JOHNSTON. They sure dealt with bonuses.

Secretary HODEL. They didn't touch on the issue of taxes.

Senator JOHNSTON. What percentage of bonuses did he give us?

Secretary HODEL. As a matter of fact, the way I understand the court's decision is that the court concluded there had been enhancement of the value on 9 tracts out of 41. There had been enhancement of the value of the Federal lease and the bonus had been increased as a result, and the court provided that 50 percent of the increased value——

Senator JOHNSTON. Precisely.

Secretary HODEL [continuing]. Should be paid to the State. That calculates to 27 percent, as it turns out, of the proceeds. And I think that may have been in the mind of the committee when it suggested, as I quoted, that 27 percent of the rents and bonuses and the interest on them should be included.

It was very clearly the intention of the committee to achieve a settlement. If you have to do the calculation, by the way, 27 percent is almost exactly halfway between 16⅔——

Senator JOHNSTON. But it sure isn't halfway between 1 to 4 percent, and the 1 to 4 percent simply disregards the law, doesn't it?

Secretary HODEL. And may I emphasize that we are not suggesting that 1 to 4 percent is where this should come out. What we are suggesting——

Senator JOHNSTON. Well, you put it on the board, and then you put 16⅔ on the board. Now, why put all that up on the board?

Secretary HODEL. May I explain why I thought I did?

Senator JOHNSTON. Uh-hmm.

Secretary HODEL. The reason I did is I thought it was important for the committee to understand the history of that. For years we were at an impasse because the most the Federal Government, under both Republicans and Democrats, would offer under the 1978 OCS Lands Act was 1 to 4 percent, because that was their interpretation.

Secretary Clark made a giant leap to 16⅔. It resulted in a counterproposal, and that has resulted in the Congress suggesting the midpoint of 27 percent. And what we are now talking about is the crucial issue of 27 percent of what.

Senator JOHNSTON. Let us get back to this question of drainage.

Senator WARNER. Could the Senator clarify the court decision? Is this a lower court? Was it appealed? Is it a district court?

Senator JOHNSTON. Actually, there are two court cases, but only one full decision. That is the one in the Federal district.

Senator WARNER. But it is on appeal, as I understand it.

Senator JOHNSTON. Oh, that is right.

Senator WARNER. Well, that wasn't clear.

Senator JOHNSTON. Oh, sure it's on appeal.

Senator WARNER. Well, I understand that, but it wasn't clear.

Senator JOHNSTON. There's another case on it, the *State of Louisiana* v. *James G. Watt,* and that case has gone only to an order on, I think it's summary judgment, which says in section 4: "Drainage is not the sole criterion for determining the fair and equitable distribution of revenues required by 8(g)(4)."

Secretary HODEL. And that we believe is more than compensated, Senator, and I think that it is important to recognize that. Taking that as acceptable, the administration offered 16⅔, which was way

above any drainage figure, perhaps as much as 15 times higher than the drainage figure we could come up with.

The counter was 37½, and the proposal was 27 percent. If we can deal with this percentage, I don't think there's a dispute over the percentage.

Senator JOHNSTON. There is a dispute on whether it is only drainage. Do you admit it's not limited only to drainage?

Secretary HODEL. I don't think there's any question that the statute was intended to be limited to drainage. One of the points we make strongly on appeal is that the court is egregiously wrong on that subject.

We do not have to conclude that, however, if we agree that 27 percent is the appropriate level. Then the issue is what should the size of the pot be and that is what I think we really should talk about.

Senator JOHNSTON. You recognize that courts, at least so far, even though they are on appeal, that the courts are against you on these questions?

Secretary HODEL. I recognize that the court gave an opinion which said that we should pay a percentage of the enhancement. That is an interesting ruling if it holds up on appeal because it does not take into account the countervailing enhancement of leases in States' waters.

Senator JOHNSTON. I think the answer to my question was yes.

Secretary HODEL. I would say it's a qualified no. [Laughter.]

Senator JOHNSTON. All right. You also said in your statement here that we were trying to expand the fund to include royalties. Now, you don't really mean "expand the fund to include royalties." The statute plainly says royalties, does it not?

Secretary HODEL. I am not aware of that.

Senator JOHNSTON. Quoting from 8(g)(4):

Notwithstanding any other provision of this act, the Secretary shall deposit in a separate account in the Treasury of the United States all bonuses, royalties, and other revenues attributable to oil and gas pools.

Secretary HODEL. "Attributable to oil and gas pools." No question. That's the drainage question and that distinctly relates to drainage pools.

Senator JOHNSTON. My question was with respect to royalties.

Secretary HODEL. My answer is with respect to pools.

Senator JOHNSTON. We can talk about pools later. Just answer the first question. [Laughter.]

My question was, in your testimony in chief you said that we were trying to expand this fund by including royalties, and I just quoted from the statute and said the statute plainly includes royalties.

Secretary HODEL. Let me emphasize, in the administration's proposal and in my prepared testimony, which goes into much more detail than I felt I could do with the time constraints, we point out we do propose royalties on a drainage basis be included in the accounts. So we are consistent there and I think would agree.

When I say royalties the expansion involved is on all of that other land that has no connection to the State, that has no pool

intersecting, and that is by far the largest share. We estimate $4 to $6 billion in future royalties that would be affected.

Senator JOHNSTON. By the way, in your statement you say that it is about $18.5 billion for the California share, is that right?

Secretary HODEL. $18.5 billion?

Senator JOHNSTON. Excuse me, $18.5 billion for royalties from 8(g) off California.

[Pause.]

Secretary HODEL. That is an estimate of the gross production value off California.

Senator JOHNSTON. That is 8(g).

Secretary HODEL. For blocks that are in or partially in the 8(g) area.

Senator JOHNSTON. Is this the area that you made a preliminary agreement to put off limits from drilling to the year 2000?

Secretary HODEL. I assume that would include these tracts, on the presumption that they would be permitted to be included successfully without a moratorium.

Senator JOHNSTON. You were going to put tracts where you have revenues of $18.5 billion off limits?

Secretary HODEL. I am advised that those are for existing leases that are not affected by the moratorium. I need to correct that prior answer. I wasn't aware of the basis of that calculation.

Senator JOHNSTON. Existing leases? Are you going to have $18.5 billion?

Secretary HODEL. I'm told that that's existing leases in the 8(g) area, a very rich harvest. What that raises questions about is how much would be included in the moratorium if this committee and the Congress permits the moratorium to continue.

Senator JOHNSTON. Do you really have real studies as to what kind of production you have out there? I mean, I am looking at the latest thing we could get, which is Federal offshore statistics published in September 1984, which says, for example, that you have 10.1 billion barrels of oil off the Atlantic. I was glad to hear that. I'm glad to hear that the Atlantic is such a rich area.

Is that the same degree of expertise that you use to estimate off California?

Secretary HODEL. I'm advised this particular number is based on estimates from plans submitted by companies on existing leases so they have a somewhat higher level of expectation of accuracy than the figures that——

Senator JOHNSTON. Were these published somewhere?

Secretary HODEL. The reserve estimates are proprietary, but we can provide the committee with the aggregates of those estimates.

[The information follows:]

Projected recoverable reserves of oil and gas believed to be located within 3 miles of the seaward boundary of California. Developed from submitted and anticipated development and production plans.

1985		1990		1995		2000		2005		2010		2015	
OIL	GAS	OIL	GAS	OIL	GAS	OIL	GAS	OIL	GAS	OIL	GAS	OIL	GAS
54.9	30.4	124.8	116.9	89.9	153.5	37.1	73.0	16.8	32.6	6.5	16.3	0.8	2.7

*OIL in thousand barrels of Oil per day
**GAS in million cubic feet per day

Senator JOHNSTON. We've been trying to get some of these answers for a long time. For example, you say in your statement that the relationship between bonuses and royalties is 2½ to 1. That is, the royalties will be 2½ times the amount of bonuses.

But what we have been given by the Department of the Interior as a rule of thumb is that royalties equal 50 percent of the present value of bonuses. Is that right?

Secretary HODEL. Senator, I think what I should do with your permission is ask these people who put the numbers together to come up and try to explain the basis, rather than my trying to relay them, if you like.

Senator JOHNSTON. Let me just ask, is the present amount of royalties 50 percent that of bonuses? Is that a working rule?

Secretary HODEL. That would be a discounted value figure.

Senator JOHNSTON. If you start off with the $18.5 billion off California, which is the figure——

Secretary HODEL [continuing]. Which you have to discount, which you would then discount.

Senator JOHNSTON. And then you get State revenues of, say, $4 billion. Then you have to discount that by about five times, don't you, to get present value?

Secretary HODEL. Yes, and if I may anticipate, the $6 to $12 billion figure that I have there is not a discounted figure, because it is very difficult to project when and at what rate those revenues will come in. That is the total gross impact, and if you discount that over a 30-year period, and some of those are well down the road, it would be a lower figure.

Senator JOHNSTON. Instead of $4 to $5 billion, it would be about one-half of a billion dollars.

Secretary HODEL. It depends on the rate at which it comes in. If it were deferred, it would be even less.

Senator JOHNSTON. Using your figures, using your proportions of 2½ to ½, that would be a relationship of five times.

Secretary HODEL. My staff indicates they believe it would be somewhere between $750 million and $1.5 billion, depending on the rates at which those royalties were received, but it is a lesser sum.

Senator JOHNSTON. Depending upon whether you rely on these types of estimates. Mr. Chairman, my time is up.

The CHAIRMAN. Senator Murkowski.

Senator MURKOWSKI. I will reserve my time.

The CHAIRMAN. Senator Nickles.

Senator NICKLES. Mr. Secretary, we appreciate your interest on this legislation. I might ask a question. Why is the administration willing to pay the 27.5 percent on rents and bonuses but not on royalties?

Secretary HODEL. The 27-percent figure was a settlement proposal. The vast proportion of the money currently in the 8(g) account comes from rents and bonuses. There is a fairly small amount that has come from royalties from the common pools areas and has been deposited according to court order.

So the bulk is rents and bonuses. I am assuming that the reason David Stockman agreed with the Budget Committee to a 27-percent figure on that amount was as part of a general conclusion of the budget item. Doing this frees up something in excess of $4 billion for accounting purposes in the Federal budget, which is significant in budget deficit reduction this year.

My reason was not only because he had reached a satisfactory budget compromise, but also because I thought it would terminate litigation.

Now, when we looked at the size of the pot, royalties—we felt—are not appropriately included because there really is no relation in royalties to the enhancement argument that the court recognized and there is no basis for paying out of royalties except out of common pools in this statute, which we think is soundly presented.

Senator NICKLES. So basically you are saying on any of the 8(g) areas there should be no royalties going to the State.

Secretary HODEL. Except our proposal that royalties from the common pools be based upon the drainage assessment. In other words, as adjacent landowners would do, we would pay royalties on the drainage.

Senator NICKLES. On Federal lands onshore, how are the royalties split up on those?

Secretary HODEL. Onshore? Onshore we have a different situation because the Mineral Lands Act was intended in part to be a compensation to the States. There we have a situation where we are within the boundaries of a State.

Paying royalties on pools that are not within State waters is comparable to paying royalties to the State of Arkansas from—I probably should have picked a different State—paying royalties to the State of Texas from a pool which is within the State of Oklahoma. That is what is involved here.

There is no State land beyond that 3 miles or 3 leagues, whichever the boundary happens to be. There is no State land. The Congress said because of our concern about the risk of drainage, we will provide rents, bonuses, and royalties for areas of common pools. We are prepared to do that.

We propose to do that and in addition pay 27 percent on the rents and bonuses, which is as high as the court has gone, and we think far beyond what could be justified. But we are prepared to

settle it out and terminate it on that basis, but there is no basis for royalty payment.

Senator NICKLES. Did Judge Parker's statement address the royalty issue? Did it say that division should be made on royalties as well?

Secretary HODEL. Yes; Judge Parker did address the royalty question and did conclude that there was no basis for including funds beyond the 3 miles, I believe, in the section read by Senator Johnston.

Senator NICKLES. As far as looking at the pie, the rents and bonuses, that amount of money available for distribution right now is what, $6 billion?

Secretary HODEL. Yes; as of March 31 it was $5.8 billion. Interest and additional contributions have pushed it to in excess of $6 billion.

Senator NICKLES. But you indicate the royalties will be some big bucks in the future.

Secretary HODEL. Our undiscounted figure on royalties ranges from $4 to $6 billion. Our undiscounted figure on taxes ranges from $1 to $6 billion. If you take the high side of those plus some additional bonuses and rents, we come up with a figure which is of that magnitude.

Senator NICKLES. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Warner.

Senator WARNER. Thank you, Mr. Chairman.

Mr. Chairman, I have an open mind on this question. It will require some study, but in the event it comes down to a very close balance, we must take into consideration the Federal deficit, and I want to clarify your figures. Under the 27 percent, the $600 million is already committed. That is money the Federal Government will have to go out and borrow as they do other financing. Is that correct?

Secretary HODEL. If I understand the numbers correctly, 27 percent of the account as we calculate it would run about $1.4 billion. That is the amount we would have to go out and finance in order to pay.

Senator WARNER. Let me reask the question. Looking at this issue from the perspective of the Federal budget deficit, would you indicate the obligations on the United States to finance this program?

Secretary HODEL. Under our proposal and what we think conforms to the committee, it would be $1.4 billion, and there would be a countervailing credit in excess of $4 billion which the Congress could include for this year. It would be a one-time withdrawal.

The CHAIRMAN. Can I interject a question? How is it possible the Government has to borrow money to share revenues if they have placed that money in escrow?

Secretary HODEL. Because the effect is, when the money is placed in the U.S. Treasury as a bank, the Government is able to work off that account.

The CHAIRMAN. Do you mean they borrow the money?

Secretary HODEL. They borrow the money in order to—to put it differently, they do not go into the market and borrow that money.

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They are able to utilize it, and when the time comes, there will be the necessity to fund that by borrowing or tax receipts.

The CHAIRMAN. But you are observing the mandate of the court to place it in escrow.

Secretary HODEL. Yes.

The CHAIRMAN. And it is in escrow.

Secretary HODEL. It is in escrow.

The CHAIRMAN. So it is whether the Federal Government is permitted to use the State's money or they have to get it out of the market.

Secretary HODEL. But the escrow account is in the Treasury and the effect is that we are not required to borrow.

The CHAIRMAN. Similar to the argument used whether or not the Federal Government has diverted Social Security money.

Secretary HODEL. I suppose it is. That is not my department either.

[General laughter.]

Senator WARNER. Let's just take one figure, fiscal year 1986 or 1987. Pick one or the other. What would be the impact? I mean, we are in a crunch right now, so we are looking at these 2 fiscal years.

Secretary HODEL. As I understand it, in 1986, the budget impact would be that the Congress would credit in excess of $4 billion, I think it is about $4.2 billion, as receipts out of this escrow account, and we would expend $1.4 billion under our proposal to the States, distribute $1.4 billion to the States, and technically, I think, in order to fund that $1.4 billion distribution, there would be $1.4 billion somewhere in the Federal borrowings that would have to be acquired.

Then let me say in the next fiscal years there would be whatever effect 27 percent would have on future bonuses and rents that were received and royalties from common pools.

If we went with the proposal before the committee—this now gets complex, because we don't have all of the money in the escrow account that would be required under the committee's proposal.

We have $5 or $6 billion in the account, and there is $7.5 billion that would be required under the committee proposal. We would have a $1.6 billion borrowing responsibility because we have about $200 million additional in the account that we could expend, and then there is the proposal before the committee that we would fund the remaining $400 million we owe of that $600 million figure out of what is called a recoupment fund, and we would in fact surcharge our collections in the 8(g) areas for a period of time by 10 percent. We would add 10 percent to that so we would accumulate the other $400 million, and we could distribute that.

Senator WARNER. If I may, I am using too much time. I would suggest that you very clearly clarify the impact on the next three fiscal year budgets of the proposal, and allow my distinguished colleague from Louisiana to put in whatever rebuttal is necessary, because I think some Senators will look at this issue purely in the context of what is the impact on the fiscal policy of this country.

Senator JOHNSTON. Would the Senator yield?

Senator WARNER. Yes.

Senator JOHNSTON. Did I understand the Secretary to say that with $5.8 billion in escrow, that in order to pay the States $1.6 billion of that, you have to borrow that money?

Secretary HODEL. Senator, as I say, this is not my department, but it is my understanding that the Treasury account, which is an escrow account, credits the receipts from the OCS in accordance with the accounting calculations. In fact, because that money is in the Treasury account, it is not separated out—you don't have a stack of bills in there. It is nominally invested. Interest is calculated on it.

Senator JOHNSTON. You got this money from oil companies. It was real money when you got it from the oil companies. Do you mean when it is put in the escrow account it is no longer real money. It is no longer bills. Therefore it is not real? It just disappears?

Secretary HODEL. Senator, as I understand it, it is an accounting entry that evidences that there is now in excess of $5.8 billion in that account. We calculate and accrue interest. But no more than my savings and loan association or bank actually holds the money in that account for me, but rather circulates it and uses it and secures it with some amount, do we actually hold those bills. We don't keep the first dollar ever paid in royalty. We use it. We will have to go out and fund that one way or another in the expenditure of the money.

Senator WARNER. Mr. Chairman, I only ask that this issue be sufficiently clarified. If necessary, we will invite the Secretary of the Treasury to introduce a statement, or the Office of Management and Budget, but let's get it clear what the fiscal impact will be. I thank the chairman.

The CHAIRMAN. Thank you.

Senator Bumpers.

Senator BUMPERS. I was here, but just for my reedification, can you restate the legislative history behind the 8(g) lands? Were they established for drainage reasons?

Secretary HODEL. I think it is clear, Senator, not only from the language of the statute but from correspondence between Representative George Miller of California, in March 1977, and Secretary Andrus that it was clearly intended to be drainage.

Mr. Miller raised the question that it wouldn't be fair with this accelerated OCS Program that was contemplated for rapid development on OCS lands to drain adjacent State resources. Secretary Andrus responded with a legislative draft and included this statement in his letter of May 10, 1977.

He said, "We favor a provision which gives coastal States fair and equitable compensation for oil and gas which is produced through wells in Federal areas adjacent to them, but which is derived from State lands." In other words, it meant if the pool crosses the State-Federal boundary and there is drilling on the Federal site.

He said they should get fair and equitable compensation. That seemed to us to be very clear. That is the interpretation. I believe I made this comment before your arrival, but that is the point I made there about the blue line.

Historically, Republican and Democratic administrations have offered between 1 and 4 percent based upon geologists' estimates of how much drainage took place. A year ago we began a new process which was to cut through this Gordian knot, and we came up with these figures.

Senator BUMPERS. Is there any legislative history indicating that the fair and equitable distribution of these revenues ought to be for the purposes of mitigating coastal impact or lost aesthetic values or environmental values?

Secretary HODEL. Senator, I could not say that there was not, but I am not aware of it.

Senator BUMPERS. I assume that in the past the Interior Department has actually leased some lands on behalf of the Federal Government and the States, where the tract crossed into the 3-mile territorial limits of the State. Is that correct?

Secretary HODEL. I believe we do not cross into the State areas.

Senator BUMPERS. We do no leasing in lands where there are common tracts? Is that correct?

Secretary HODEL. We do no leasing into the State waters.

Senator BUMPERS. Do you allow the States to do any leasing in Federal waters, into the 8(g) areas?

Secretary HODEL. No; if I may show this map, this green line is the State shore. This is the Outer Continental Shelf limit.

Senator BUMPERS. That is the State's 3-mile limit?

Secretary HODEL. This is the 8(g) line, this blue line here. We lease only up to the State line. The State leases only up to the Federal line. We believe the fair intent of the statute originally was only pools such as these which were intended to be reached by 8(g). We have gone far beyond that in our proposed settlement, and we are now being perhaps dragged further.

Senator BUMPERS. Mr. Secretary, referring to the illustration of the pool on the other side of the chart, if the State leased their part of the pool, and you leased your part, you are obligated to pay them under the law some fair and equitable amount of what you get out of that pool. Is that correct?

Secretary HODEL. That is our interpretation.

Senator BUMPERS. Are they under any obligation to pay you for their share?

Secretary HODEL. Not that I am aware of. It has been a one-way proposal.

Senator BUMPERS. Let me just ask you what is the logic behind this? If that tract is being drilled on both sides of that line, one side under Federal leases and the other side under State leases, there can't be any drainage there, can there?

Secretary HODEL. Normally if you have drilling on both sides of the line, and if placed appropriately, there would not be a drainage problem. The problem usually arises where there is drilling only on one side of the line.

And there was in fact some discussion about the concern that this would force the States to lease aggressively where they weren't intending to lease in order to prevent drainage.

And the suggestion was, we can solve that by providing that the Federal Government pay a royalty on drainage, so the State wouldn't be required to drill that tract or to lease that tract for

drilling forthwith. I think the logic was, the fear was we would have an aggressive, successful Federal program which to some extent we have had.

Senator BUMPERS. Now, move on up to the outer edge of the 8(g) lands shown on the map. You have one pool there that extends into both. Now, in a situation like that, I assume the Federal Government leases both sides of that line.

Secretary HODEL. We leased the entire tract C, which is the 3- by 3-mile square here.

Senator BUMPERS. Let me ask you this. Why would you not lease there the same way you do in the other situation? But of course you can't know where the pool lies until after drilling has taken place, can you?

Secretary HODEL. This is all Federal water.

Senator BUMPERS. What I am saying is, how can you prorate revenues from a pool which has probably not been defined when you are drilling outside the 8(g) area and inside the 8(g) area? How will you distribute that money?

Secretary HODEL. We think that if the statute were followed, there would be no proration necessary here because this pool does not in fact intersect the State boundary at all, but that has been set aside by our agreement to settle at 27 percent of what is in here.

The biggest argument on dollars is whether all of the bonuses, rents, and perhaps royalties from this tract would be deposited. Since 1984, we have broken the tracts at this line and we will not have this proration problem any more. We would not have a tract C which intersected both zones. This would be outside.

Senator BUMPERS. You now define leases which are either inside or outside the 8(g) areas.

Secretary HODEL. Yes, but prior we did not do that, and a very significant sum of money is involved as a result.

Senator BUMPERS. Is that a satisfactory arrangement with the States?

Secretary HODEL. I would have to say probably not. I think the States' view is anything that reduces the amount of money they receive from the OCS is not satisfactory.

Senator BUMPERS. Now, listen. I used to be a Governor, and I understand that argument.

[General laughter.]

Secretary HODEL. But the coast of Arkansas has had very little opportunity for this.

[General laughter.]

Senator BUMPERS. We haven't gotten a dime out of our Outer Continental Shelf lands.

Secretary HODEL. But you have received a significant amount of money out of the proceeds of the OCS which go into the general Treasury, and you will have less if this proposal before the committee goes forward rather than the proposal that we have been supporting.

Senator BUMPERS. Mr. Secretary, I was reading Governor White's testimony this morning. I don't want to preempt him, because I assume he will testify here in a little while. He mentioned the taxes that the Government is collecting off this land, which I be-

lieve he said represents as much as one-third of all of the revenues from it. He feels that that money should be shared. What kinds of taxes are we talking about? Are those windfall profits taxes, severance taxes, or other taxes?

Secretary HODEL. We have assumed it would include windfall profits tax and Federal corporate income tax. By the way, that presents an enormously complex issue because how do we or anybody make a determination of how much of the tax paid by a particular corporation comes from a particular tract somewhere off the coast of America when they have hundreds of tracts and thousands of wells.

It is an opportunity for litigation that is unending, and if all else fails, I would hope that the committee—if it decides to do something like that, which would be, I think, absolutely precedential, I don't know of another circumstance in which a share of Federal taxes has been identified in this fashion and will have to be calculated in this fashion.

I hope that the committee will not leave us to interpret what in heaven's name that means.

Senator JOHNSTON. Would you yield?

Senator BUMPERS. Sure.

Senator JOHNSTON. It was not our intention to include taxes. We intended clearly to set at rest the tax issue, and while we think we have a very good argument for the court on the question of taxes, as Governor White's excellent statement shows, we intended to put that at rest. Perhaps that was not clear from the legislation. We will make that clear so that that is no longer a question.

Secretary HODEL. The language of concern, in addition to royalties, is "other revenues." We have difficulty locating any other revenues other than taxes.

Senator JOHNSTON. We are willing to clarify that.

Senator BUMPERS. Mr. Secretary, I understand you have no objection to the 27-percent share formula proposed for the escrow account as it exists right now. Is that correct?

Secretary HODEL. That is right. We have agreed to that.

Senator BUMPERS. Even though that is more than has ever been offered before.

Secretary HODEL. It most assuredly is, but we felt that the settlement and the extinguishment of litigation as stated in my testimony was worth it. Let's get this behind us and move forward.

Senator BUMPERS. Are you prepared to tell this committee how you think the Johnston-Murkowski issue is flawed insofar as the distribution of future revenue is concerned? Let's assume we can resolve the sharing of the money there now with the 27-percent formula. Are you prepared to tell us how you would distribute these funds in the future?

Secretary HODEL. Under the Johnston-Murkowski proposal?

Senator BUMPERS. Yes; what do you find most offensive about the Johnston-Murkowski proposal?

Secretary HODEL. We have apparently resolved the tax issue. That would change my $6 to $12 billion figure. It would look more like $4 to $6 billion.

Senator BUMPERS. All right.

Secretary HODEL. The most significant dollar effect over time would be the effect on probably royalties. It would provide that we would pay 27 percent of this royalties. There is no basis that I can see in history or otherwise for paying a royalty from the Federal waters as illustrated in that map except where there is a common pool and drainage.

That would be the most direct effect, and there would be something in the neighborhood of $100 or $200 million a year that we would estimate for the next 30 years in royalty payments. They would not be even. They would fluctuate as wells came into production. That would be the most significant cost in most of these areas. Off some States the bonus payments could become quite significant, but that is problematical because we have the issue of the moratorium off California and the lack of finds off the State of Alaska. That would be the downstream effect.

Senator BUMPERS. Thank you, Mr. Secretary. My time is up.

The CHAIRMAN. Senator Hecht.

Senator HECHT. Thank you, Mr. Chairman, no questions.

The CHAIRMAN. Senator Evans.

Senator EVANS. Thank you, Mr. Chairman.

Mr. Secretary, one of the questions around which this seems to revolve is the question of fair and equitable distribution or division. That's not defined in the statute. The proponents, it's my understanding at least, suggest that "fair and equitable" means 50 percent.

Do you have any alternative view as to what "fair and equitable" might mean?

Secretary HODEL. I think the concept that properly should have been in the minds of Congress in 1978—and I don't know what was—is, as with two adjacent landowners in an oil field, there ought to be some mechanism for sharing where one's resource is being tapped by the other.

That is clearly what is in the legislative history that I have referred to, the correspondence between George Miller, the Congressman from California in 1977, and Secretary Andrus. It clearly talks about production from Federal areas adjacent to the State, but which is derived from State lands.

That seems reasonable and proper, and I think in the context of 1978 that makes sense.

Senator EVANS. It does seem to me that if the Congress at the time they passed this law had meant equal, they would have said equal. That is an easy word to use if equal is what is meant. Fair and equitable, it seems to me, has quite a different connotation.

You stated in your written testimony that you are opposed to the information sharing requirements in the markup vehicle. We haven't talked about it in the oral discussion we have had. Can you explain a little more about that and what kind of data would be made available if this provision becomes effective?

What is the downside and what is the importance of that provision?

Secretary HODEL. Let me say that today we make available to the States for review all information which we have on the 8(g) area from all sources that we have, provided that the State indemnifies us from the loss or distribution of proprietary data because

we have proprietary information in this. So we do now make it available.

This is an incredibly broad provision. It says we are mandated to provide the Governor "all information from all sources concerning the geology"—it is not limited to information in our possession. It is not limited in a way that gives us any confidence that we could resist a lawsuit claiming if we had to go out and produce additional information for the benefit of the States.

We think there is already an appropriate information requirement which we are meeting. And we have had a problem with some States that could not indemnify us. They wanted proprietary data and we could not give it to them without indemnity. Some States, most States, have now resolved that.

Senator EVANS. On the question of future potential cost to the Federal Government, that $6 to $12 billion apparently, from Senator Johnston's offer, is now down to about one-half that if you leave taxes out. Does that all arise from already existing leases?

I mean, you testified that there would be no future proration because you do not intend to have cross-boundary leasing.

Secretary HODEL. I am assured that that $6 to $12 billion or the $4 to $6 billion of royalties which is that share would be all from existing leases. And let me say, if the committee decides to go forward and exclude taxes, it needs to be done carefully with proper language.

All through the correspondence with the Governors, all through the hearings and debates on this issue, taxes have been raised again and again as an appropriate source of revenue for this account, and I hope the committee will not leave any ambiguity and force this back into litigation.

Senator EVANS. It seems to me we are zeroing in at least. I know there are several other elements that are at least not directly monetary in nature which are included in the draft or the markup that the chairman has submitted. One of them is the information element.

There are several others, but I think the key is really the question of that future amount of money based on already existing leases, and it's a question of whether States deserve some share, some considerable share, it appears to me, of oil that is drawn from lands that do not even touch or come close to touching State boundaries. Is that correct?

Senator JOHNSTON. Would the Senator yield at that point so I can clear up this question of information? The present law provides that the DOI share "all information concerning the geographical, geological, and ecological characteristics of such regions."

And the problem is that they have failed to comply with that. Judge Mentz in his decision on the *Louisiana* case stated: "The Secretary of the Interior failed to comply with the information sharing requirements outlined in 43 U.S.C. 1337(g) (1) and (2)."

That is the reason we had to tighten up this information sharing. They simply haven't complied with the law.

Secretary HODEL. May I say that counsel informs me, Mr. Chairman, that we feel that that conclusion is not justified and it will certainly be, following final judgment, subject to appeal.

Senator JOHNSTON. These courts are a real nuisance sometimes. [Laughter.]

Senator EVANS. I would just say, I am not sure the Secretary had a chance to finally respond to the last question, which was——

Secretary HODEL. May I say that, with the proposal before the committee, we have listed a number of things. There's a recoupment provision, which is this additional 10-percent surcharge on future bonuses until we've collected approximately another $400 million to pay that $600 million.

There is no extinguishment provision. The language is not clear. It leaves an option to the States as to whether they would sue us or accept this amount of money. And there are some States with such a small amount of money in this account that they might conclude they would be just as well off to take this as a base, not accept the money, and sue further.

We think we should eliminate the litigation with whatever the Congress finally chooses to do. The tax revenue question we have eliminated. We are concerned about the information.

The interest rate called for is the highest available. I have discussed that in my testimony. We have generally used the Treasury rate in calculating interest. This would require a calculation of an investment at a much higher return.

The CHAIRMAN. We have a very severe time problem. There are four other members of the committee who have not had an opportunity to ask questions. I will try to divide the time between now and the time the Secretary has to leave so that each member may have at least an opportunity for a first round of questions.

Mr. Secretary, would it be possible for Mr. Bettenberg and Mr. Wiles or both to remain in the event of further questions?

Secretary HODEL. Yes, Mr. Chairman. And I would like to offer to the committee the additional staff who are here, who have actually done the calculations. So that if you want to get into the details, you can do that.

The CHAIRMAN. Thank you very much.

Senator Domenici.

Senator DOMENICI. Mr. Secretary, I think we have at least two issues. One is how do we comply with the reconciliation instruction; and the second is, it is the Senator from Louisiana's desire, and frankly I share it, that if we're going to draw a statute—and that is what we are trying to do here; this is going to be statute law—if we're going to draw one, that we ought to here and now present from this committee to the Congress a total settlement of this issue wherever the matters are unclear.

So it seems to me that that ought to be our prime motivation, not necessarily what the House Budget Committee had in mind, not necessarily what the Senate Budget Committee had in mind, other than as it relates to making sure that the baseline budget calculation yields $4 billion. And I don't think anything that is being discussed is going to violate that.

And second, that over the 3 years we not—that we come out with at least a savings of $1.4 billion, which is the sum total of 3 years' actions. That is what the budget resolution asks us to do. That means in the second and third year it costs you money, but the

sum total of the 2-year costs are exceeded by the 4-year costs, in that amount of $1.4 billion. I think that is one thing we have to do.

But beyond that, we have to resolve all of the issues. Now, it seems to me that, whatever Dave Stockman said in his letter about the baseline numbers, it wouldn't necessarily resolve all of the issues. We ought to resolve them here.

Now, as I understand it we have no problems in the first 3 years budgetwise under the Johnston proposal. So we start with that. The outyears create a problem for us to determine in terms of whether in this settlement we are doing more than the statute logically permits in a settlement, or that we as a committee conclude is a logical way to settle the differences.

Is that a fair statement of what you would agree we ought to do?

Secretary HODEL. Yes; when I opened, I commented that this is a budget issue and the committee, the Congress, is free to do what it chooses.

Senator DOMENICI. So you would prefer that we resolve the issue, rather than distribute enough funds to meet a budget resolution?

Secretary HODEL. Absolutely.

Senator DOMENICI. Give me one more time why you don't think—aside from the substantive issue, why you think the proposal before us, the pending amendment to resolve all of these disputes, will not resolve all of these disputes?

Secretary HODEL. The biggest reason initially was the litigation over what the term "other revenues" meant. Apparently the committee would make plain that it does not mean taxes, and perhaps the other revenue provision could come out and relate to royalties, bonuses, and rents only.

Senator DOMENICI. That's one. We may already have that one.

How about recoupment?

Secretary HODEL. I am concerned about the information provision being overly broad and putting demands on us for information we may not be able to provide.

Senator DOMENICI. Clearly that's an issue, but a lesser issue. What is the recoupment litigation that you spoke of?

Secretary HODEL. The recoupment provision is not one which I believe would generate litigation.

Senator DOMENICI. Your staff is saying yes or no? I cannot tell. [Pause.]

Secretary HODEL. The recoupment provision, because it says we would restore to the fund and would pay from what should have been deposited to the account, opens up the argument as to what should be.

Senator DOMENICI. So it seems that clearly, if we want to resolve this, we should resolve that issue of what should have been deposited with clarity, so that when they take this recoupment add-on, if we vote it in, that is all they're going to get.

Secretary HODEL. It would be better to have a specific number.

Senator DOMENICI. If all that's done, what remains, as I gather, is it is the outyear issue beyond the 3 of a possible drain on the Treasury that you believe shouldn't be there on the royalty issue?

Secretary HODEL. That's correct.

Senator DOMENICI. That is one of the big ones.

Secretary HODEL. And realistically, the 27 percent of rents and bonuses would represent a full and fair settlement of this issue beyond anything that I think the framers would have thought was coming. But the committee is free to make that decision.

Senator DOMENICI. I am assuming we are going to do that, because there's too much evidence around, if you are settling and we are trying to reduce the settlement, that somehow the settlement got resolved at around 27. What then remains, the outyear royalty issue and?

Secretary HODEL. The surface acreage proration question.

Senator DOMENICI. The outyear 8(g) sharing issue.

Secretary HODEL. We will try to avoid that by not leasing across the edge of the 8(g) boundary.

Senator DOMENICI. I know my time is running out, but let me ask you now—if you did in your testimony, in your written testimony, don't tell us again because we will get it before markup. We have to settle those issues. If my premise is that the committee wants to settle the issues, what's wrong in your opinion with the royalty issue as presented in the Johnston proposal and interpretation of the statute?

Secretary HODEL. I think the interpretation of the statute is clear. It would be a decision of this committee that it wants to change that statute, and I would think that would be unjustified, unsupportable, except if it seemed appropriate to the committee. But I don't think there's any basis for paying royalties on pools that do not intersect State waters.

Senator DOMENICI. So consistent with settling within the logical framework of what exists, we have to decide whether you are right on that issue or whether the proponents of the bill are right in terms of us settling a dispute. It is a dispute, is it not?

Secretary HODEL. It is a dispute, most surely.

Senator DOMENICI. You said it wasn't a question of interpretation, but I don't know how it could be a dispute if there's no interpretation issue.

Secretary HODEL. I think the history is fairly clear of what was intended by the Congress, based on what made sense in the context of oil and gas activities. But what we are now dealing with is a framework created by settlement discussions.

There's one other item I should mention that is troublesome to us in the proposal. It eliminates the anti-injunction provision so that if a State would disagree with our proposal in the future on an OCS sale, whereas today they cannot enjoin us from the sale provided we deposit moneys in this account, my understanding is they would be able to seek injunctive relief in the future. That would not be in the best interest of the program

Senator DOMENICI. It would seem to me if this gets resolved in their favor that they ought to be willing to concede on that. They ought to be more willing to have offshore leases if this is the bonanza that you believe it is, or the settlement on the high side, is perhaps the better way to say it.

All right, one more time. In addition to the royalty and recoupment settlements, so that that is clear, and the injunction issue, is there one other disputable item in the outyears that is major?

Secretary HODEL. There is language used in that bill that talks about the hydrocarbon area. That is not a defined term and it could result in further complications in our trying to figure out what zone we are sharing revenues for.

Senator DOMENICI. Thank you very much.

The CHAIRMAN. Senator Wallop.

Senator WALLOP. Thank you, Mr. Chairman.

Mr. Secretary, I have two observations. One I think goes to my colleague from Washington. Probably the reason they chose the term "fair and equitable" instead of "equal" is because it's a better lawyer's word. There are certain other revenues that we share around this country that are unmentionable but obvious.

Let me suggest that there is sort of an aura of illogic or incompleteness about the department's position. On the one hand, you protest like hell—and I think legitimately—this mindless moratoria that Congress continues to set in place offshore of the United States, without hearings or anything, simply by amendments. But on the other hand, by protesting this royalty arrangement you have removed in essence all of the incentive any State might have for having at least a political dialog, a political resistance somewhere within the State, to these moratoria and ensure political support for them.

And that seems to me to be shortsighted, both in terms of the long-term Federal revenues and in terms of American energy production offshore.

Secretary HODEL. May I respond? When I began my testimony this morning, I emphasized that I was more relaxed about this proposal than some because this is not a national interest question; it's a budget question. It's not like the moratorium, which I think strikes at the heart of the national interest on the OCS Program and our energy supply.

Second, by no means does this settlement represent a removal of all of the incentives. This 27 percent which the committee has mandated and to which the administration agrees and supports represents to the State of Louisiana in the worst of cases nearly $500 million.

Senator WALLOP. It does support——

Secretary HODEL. We do support 27 percent of a $5.8 billion account as of March 31. We favor that and would like that to go forward.

What we're talking about, Senator, is the part in the red. How much bigger are the States of Louisiana, Texas, and California going to make this pot out of the pockets of the rest of the taxpayers and citizens of America from the Federal resources?

By the way, I have been a general proponent of revenue sharing with the States and have even suggested that I hope localities get revenue sharing, because I think it would do precisely what you say. But that is not what the issue is here.

The issue is what is fair and just. It would be a small amount. We have agreed to a settlement of a large amount, significant dollars. But it's now being expanded by the way in which the pot is calculated.

Senator WALLOP. But I still find your argument in the letter of September 20 to be slightly ironic. In the third paragraph of it on

page 2, you point out that the onshore and offshore leasing programs cannot be equated because the 1920 Mineral Leasing Act was specifically designed as a revenue sharing measure.

Yet, every year the budget request from your department denies the existence of that interpretation of the act by requesting that the States' share of these mineral receipts be adjusted from a gross to a net covering administrative costs.

What is even more curious is that the department rationalizes this adjustment of the onshore States' share by making the claim that the offshore program doesn't require as much work, even though the offshore revenues comprise 80 percent of the total. I am a little lost in consistency.

Secretary HODEL. Senator, if the committee does what is proposed by the Senators from Louisiana and Alaska, the problem will be exacerbated and not improved because the reason we are in the position we are in is efforts to find ways to reduce our costs and increase the Federal revenues. Because the Mineral Leasing Act of 1920 clearly requires us to do what we currently do, we are requesting that the Congress reconsider that. We have not been enormously successful as you, I am sure, would point out.

But on the OCS, we have never been in that position. And if we now go this route, it is just that many more hundreds of millions of dollars not available to the Federal Treasury that would be distributed essentially to three States.

Senator WALLOP. But they might indeed be more or less available if you got rid of some of the moratoria and began to find some production areas you are not prohibited from doing.

Secretary HODEL. In my opening statement, I said that one reason I'm more relaxed about this is that it could help in our moratorium fight. Frankly, having had some more recent experience in coastal areas, I'm not sure that's true.

Senator WALLOP. Thank you, Mr. Chairman.

The CHAIRMAN. We have two Senators who have not yet had the opportunity to ask questions, and I understand the Secretary has to leave very soon, so I will try to divide the time between now and 10:30 between the two remaining. Senator Metzenbaum.

Senator METZENBAUM. I don't have many questions.

Mr. Secretary, you may have answered this. I had to leave. I am sorry that I did. But Judge Parker's decision deals with the 8(g) lands, but specifically does not deal with that which is beyond the 8(g) area. What is your view with respect to that which is not dealt with in the court's opinion and what impact on those, on the drainage issue, do you see coming out of this legislation vis-a-vis the example that you gave of $1,000 and $9,000 as compared to $9 million?

I wish you would express yourself on that and tell us why you think this legislation should be amended to be fair to the Government as well as the States vis-a-vis just that aspect of the issue.

Secretary HODEL. The effect of this proposal would be to mean that any tract the corner of which is clipped by the outer reach of the 8(g) zone would be included for royalty payment purposes in the account, and that has the significant economic impact we've talked about. It would increase the current account from about $5.8 to about $7.5 billion.

We think that there is no basis for having done that. We think that is not appropriate or reasonable.

Senator METZENBAUM. Judge Parker did not deal with that at all?

Secretary HODEL. My understanding of Judge Parker's decision—and I am looking at Senator Johnston because he read from the decision earlier—was that he specifically said he did not deal with areas beyond the 8(g) zone.

Senator METZENBAUM. That is correct. That is correct, he did not. Therefore, my question to you is——

Senator JOHNSTON. If the Senator would yield at that point.

Senator METZENBAUM. Yes.

Senator JOHNSTON. What he said is he took that into account. Here is what he said, if I may digress a minute:

> Some tracts are not entirely within the 8(g) zone. See infra, finding of fact No. 7. To the extent these tracts extend beyond the 8(g) zone, they are beyond this court's jurisdiction in the sense that the court cannot distribute Federal revenues attributable to 8(g) lands.
>
> The Court has taken this factor into consideration in formulating the fair and equitable division of revenue attributable to tracts part within and part without the 8(g) zone. For future lease sales involving such tracts the Secretary should deposit in the escrow account *all* revenue attributable to such tracts because in the absence of an agreement between the Secretary and Governor the determination of what percentage of revenue is attributable to the 8(g) portion of a particular tract is a finding of fact appropriately made by the Court. Nevertheless, the Secretary can avoid this eventuality altogether merely by drawing the tract lines so that none are part within and part without the 8(g) zone.

What he did was put all of the revenues in and then, with respect to the enhanced revenue took 50 percent. So Judge Parker said he did not have jurisdiction beyond 8(g), but he took that into consideration and divided the revenues from tracts lying part within and part without the 8(g) zone.

Secretary HODEL. We do not think that is a proper holding and we will resist it.

Senator METZENBAUM. As I understand it, just one more sentence, and he is saying that that is not part of this decision: "Nevertheless, the Secretary can avoid this eventuality altogether merely by drawing the tract lines so that none are part within and part without the 8(g) zone."

Senator JOHNSTON. And they have done that.

Secretary HODEL. Since 1984 we have been doing that. We're talking about what occurred prior to the time we began doing that.

Senator METZENBAUM. Do you feel this committee could achieve the objective of the budget resolution by accepting the 27-percent figure that you are talking about and that Senator Johnston is talking about, but at the same time excluding all areas beyond 8(g), for further resolution either legislatively or by negotiation?

Secretary HODEL. I think this committee can meet the Budget Committee's objective, as Senator Domenici suggested, under either proposal. In other words, I think the Budget Committee's requirement can be met under either proposal. What we are talking about really, Senator, is whether we believe the pot against which our agreed 27 percent should be applied is a smaller or larger amount.

And our argument is that there is really no historic or geologic justification for that account to be expanded as is now being talked about.

Senator METZENBAUM. We are talking about something approximating $2 billion now, the difference between $5.8 billion and 7-point something?

Secretary HODEL. $7.5 billion.

Senator METZENBAUM. And over a period of, you said, 30 years it amounts to what, $6 to $10 billion? Am I right about that?

Secretary HODEL. We were talking $6 to $12 billion undiscounted, and that assumes the taxes question. I was assured by the Senator from Louisiana that the intention would be to make plain taxes are not included. That means the future royalties provision would be in the $4 to $6 billion range.

Senator METZENBAUM. I question whether the States have any claims on any revenues, bonuses, rents, or royalties, on tracts that lie entirely within Federal waters and which do not have common pools with State waters. But nevertheless, you have conceded the point that the States have a valid claim on rents and bonuses.

Having done that, it seems inconsistent to say that they have no claim on royalties as well. Could you explain the basis for distinguishing between bonuses and rents on the one hand and royalties on the other?

Secretary HODEL. Yes; first, there is the court case that Senator Johnston has talked about. And second, it was a settlement proposal. It was something negotiated between David Stockman, the head of the OMB, and the Budget Committee in an effort to reach an agreement, to achieve a reconciliation.

And that discussion and what shows up in the language of the committee is this language. It says: "A 27-percent share of the bonuses and rents in escrow, as well as the interest that is accrued on them." Bonuses and rents. It was a settlement.

Senator METZENBAUM. In other words, you have made a settlement; don't go back on the settlement.

Secretary HODEL. Now, the argument was: That was a neat settlement; let's expand it by a significant number of dollars absolutely beneficial to the three States involved and a few others. But there's no real basis for that and it was not the agreement.

Senator METZENBAUM. Thank you.

The CHAIRMAN. Senator Murkowski.

Senator MURKOWSKI. Thank you, Mr. Chairman.

Mr. Secretary, I understand and appreciate the posture of serving two masters, so to speak. But in going back and reviewing again the law, it seems quite clear to me that there are a couple of exceptions that we have already seen occur that, according to my interpretation, just don't relate.

And if I may review again that portion of 43 1337: "Notwithstanding any other provision, the Secretary shall deposit in a separate account." And I'm going to stop there because it is my understanding that you said that there would be a budgetary impact associated with the fact that the Government put this money out and had it working for them and didn't have it in effect in an account. And even though the 27 percent, which you have agreed now is fair, with some reluctance, $1.4 to $1.6 billion, which would be the

States' share, in effect would have to be appropriated and as a consequence have a budgetary impact.

Now, if that is the case indeed, I think there is a clear difference in the intent of what the law says. It doesn't say that you go out and spend it and then have to appropriate it back after you spend it. It implies that you have an escrow account of those funds on hand.

Now, I'm curious to know how the interpretation came about internally in the Interior Department.

Secretary HODEL. My understanding is this question was raised before the Supreme Court and the Supreme Court said the handling of this kind of account by the Treasury was perfectly appropriate [*United States* v. *Louisiana*, 446 U.S. 253, 264 (1980).]. As a bank receives deposits, it is sometimes shocking to early depositors to find out that the bank has not retained their money, but that the bank has gone out and loaned it on security.

Senator MURKOWSKI. I beg to differ with you, Mr. Secretary. There is a distinction. You have to have a reserve, you have to have an account. Someone doesn't say you can go ahead and spend it. You are using the example of a bank loaning someone else's money, but that bank doesn't loan everybody money.

Senator JOHNSTON. You're talking about S&L's. [Laughter.]

Senator MURKOWSKI. That bank has to keep some of the reserves so that it can meet the demands. You're telling us that the Interior Department has gone out and spent the money.

Secretary HODEL. No, I'm not. This money goes into an account in the Treasury.

Senator MURKOWSKI. Then there should be a reserve account set up, an escrow account.

Secretary HODEL. There is an account. Maybe the words "budgetary impact" are the wrong words. I don't know what the esoteric terms are here, but my understanding is that, because that money is in the Treasury, the Treasury has that much less borrowing that it has to do.

If we withdraw $1.4 billion and pay it out, actually to make the cash outlay will require a borrowing by the Federal Treasury $1.4 billion greater. That is what I mean by budgetary impact.

Senator MURKOWSKI. I appreciate the clarification, because the process of how the Treasury separates its funds when it has a dictate in the law that it indeed deposit in a "separate account" implies that it should not have a budgetary effect, because that money has been collected in lieu of a dictate of payment out.

Secretary HODEL. And that would account for why there would be a $4 billion benefit to the Treasury from the settlement of this matter, because money in that account——

Senator MURKOWSKI. That money does not belong to the Treasury. It's being held in trust pending future disposal. So it should not have a budgetary effect.

I realize that OMB's attitude may be different, but the realities are that this law further makes reference, I think, to another point that is in dispute: "All bonuses, royalties, and other revenues attributable to oil and gas pools underlying both Outer Continental Shelf and submerged land subject to the jurisdiction of the coastal States, until such time as the Secretary and the Governor of such

coastal State agree, or if the Secretary and the Governor of such coastal States cannot agree" and that's where we are today—"the district court of the United States determines a fair and equitable disposition of such revenues and any interest thereon."

Now we're at the Federal court in Texas. They have sustained the State's position and you are under appeal.

Secretary HODEL. They have not. Let me say, Senator, the court's decision has a number of elements in it, and among them, the court concluded it does not have jurisdiction beyond the 3 miles of the 8(g) zone. Among other things, it has not dealt with the royalties.

It has not dealt with the royalties issues at this time, and we are reasonably optimistic on that score. It has said that enhancement only is subject to this distribution, not bonuses, but the enhancement in the bonuses is attributable. That is not unlike a drainage-type argument.

Senator MURKOWSKI. Do you expect ultimately one court decision to prevail in all seven States, or ultimately could this go on to the point where each State would bring litigation within their jurisdiction?

Secretary HODEL. Ultimately if we continue on the present course we will be before the Supreme Court at least once, hopefully by agreeing that a 27-percent share of that account, which is vastly greater than anything the prior history would have suggested, was appropriate.

We thought we would reach a settlement.

Senator MURKOWSKI. We have discussed the 50–50 merits of what is equitable, and we are down to 27 percent in the application of the formula.

Secretary HODEL. No, sir. I beg to differ. We have not discussed 50–50.

Senator MURKOWSKI. Well, it has been discussed before this committee.

Secretary HODEL. You read language from the law and it said, "Revenues attributable to oil and gas pools underlying both the Outer Continental Shelf and submerged lands subject to the jurisdiction of a coastal State." That was what was the congressional intent. That is the 1 to 4 percent.

As a result of settlement negotiations, we have moved it clear up to 27 percent and have agreed. All that is at stake here today is how big the Congress is going to make this pool.

Senator MURKOWSKI. But you imply, Mr. Secretary, that it is an open-ended liability of the Federal Government as far as the future recoupment above and beyond the 27 percent of the States' formula is followed here, and that is where you object, but you counter that by acknowledging that indeed the Department of the Interior in revamping its leases will try and eliminate the exposure in the future on 8(g).

So, why on one hand do you say that you are extending substantial financial commitments of the Federal Government when indeed you have in the future the capability by drawing your leases in a manner in which you see fit so that you won't have that.

Secretary HODEL. The most significant amount to be affected by this is the royalties. We anticipate if you include royalties you are talking about an additional $4 to $6 billion undiscounted in the future.

Senator MURKOWSKI. In the future, but by the same token you are really talking about $400 to $600 million currently applicable, and that is coming out of future Federal—out of the 73 percent.

Secretary HODEL. For the $200 million, there is enough in the account for that. The remaining $400 million, I believe, would have to be made up by the recoupment.

Senator MURKOWSKI. My point is, if you follow the arithmetic, you have got to come up with $1.4 to $1.6 billion, but you have already got that theoretically.

Secretary HODEL. We are prepared to do that.

Senator MURKOWSKI It would cost you another $400 million per year currently.

Secretary HODEL. $400 million total.

Senator MURKOWSKI. To abide by the State formula.

Secretary HODEL. To abide by the committee formula.

Senator MURKOWSKI. Which is obviously the State formula, and that would come out of future Federal shares which——

Secretary HODEL. And we would have $4 to $6 billion, we believe, in royalties from existing leases which would be paid out of——

Senator MURKOWSKI. But you have that anyway.

Secretary HODEL. Well, Senator, if the committee decides it wants to pass $10 billion to these States, we have the money. As I said at the beginning, that is not the issue. If this committee wants, in its largesse, to give three or four States, if we include Alaska, billions of dollars, we have the money, but we will increase the deficit.

Senator MURKOWSKI. I am out of time. But I have one more question.

Secretary HODEL. But we are not. All that is at stake here is how you want to divvy up the pot in terms of what is fair to the taxpayers of America.

Senator MURKOWSKI. I think we have all discussed not only what is fair to the taxpayers, but what is in the best interest vis-a-vis the taxpayer being on both ends of the argument here. My last question is, Has the Department a policy of refraining from depositing in the 8(g) account revenues from tracts determined by the Department to have no hydrocarbon potential, and was there not a recent policy change in that regard, and my question is why?

Secretary HODEL. Senator, I think what that refers to is, where a tract does not have a common pool as referred to in this statute, we have recently begun not depositing those funds to the account.

Senator MURKOWSKI. Yes; but you had a policy prior to that where you did deposit.

Secretary HODEL. Senator, in some cases we are under an injunction to deposit all moneys into an account.

Senator MURKOWSKI. But did it result, your current change, has it resulted in an increase in the amount of 8(g) or a decrease?

Secretary HODEL. It would result in a decrease in the amount of money in that account. Were you here when I drew this second chart?

Senator MURKOWSKI. Yes, yes. I would like for the record to know how much the decrease was for each State which would have been a recipient.

Secretary HODEL. I will have to supply that for the record, but the gross amount would total, we estimate, about $7.5 billion in the account instead of $5.8 billion in the account. So it would be about $1.7 billion additional dollars in the account if all money were put in instead of being prorated.

[The information follows:]

Alaska, $46,503,880.19. Calfornia, $20,336,936.23. No other States were impacted.

Senator MURKOWSKI. I thank you.

I have been asked to chair the conclusion of this, Senator. I am told the Secretary is late for his plane.

Secretary HODEL. If I could come back——

Senator JOHNSTON. I am sorry the Secretary is not going to have time to find that $5.8 billion that is missing.

Secretary HODEL. It is there. Trust us.

Senator MURKOWSKI. I am glad to hear it is not going to have a budgetary impact.

Secretary HODEL. Let me say, Senators, I appreciate the chance to be here. As I said in the opening, this is a dollars and cents question. If you agree with your colleagues from Lousiana, Texas, Alaska, and California that the citizens and taxpayers in those States should get this kind of a benefit——

Senator MURKOWSKI. You use a compelling argument, Mr. Secretary.

Secretary HODEL [continuing]. As compared to the rest of the Treasury, we have no way of resisting it, but it doesn't seem to me appropriate based on the history or the record, and it would seem to me that far more important is the issue we face as we talk about a moratorium that actually prevents this Nation from finding resources that contribute funds to all of us.

Thank you very much for the chance to be with you.

Senator MURKOWSKI [presiding]. Thank you very much, Mr. Secretary.

Our next witness is the Honorable Mark White, Governor of Texas, and I believe, Senator Johnston, you might like to introduce the Governor. I must take a telephone call.

Governor WHITE. Do I have to take an oath?

Senator JOHNSTON. Governor, your integrity around this place is sterling. You don't need to take an oath. As a matter of fact, I have read your statement, and I believe every word of it.

We are glad to welcome Gov. Mark White from Texas, who has also been attorney general of Texas and has been deeply involved in this legislation and in the litigation. Governor, we are very happy to welcome you here. You may proceed as you wish. You may read or summarize your statement as you please.

STATEMENT OF HON. MARK WHITE, GOVERNOR OF THE STATE OF TEXAS

Governor WHITE. Thank you very much, Senator Johnston and members of the committee.

I think just as an introductory statement to the parting remarks of the Secretary and the concerns I know every member of this committee as well as Congress has about the proper resolution of this matter.

Every single concern that has been raised today by the members of this committee over where is the money coming from, had the Secretary and the Department of the Interior followed the law and the court's instruction, we wouldn't be talking about that now, because the money would have been in an escrow account, and would not have been taken out, and it would not be a question for this committee to decide where the money is coming from.

I appreciate your invitation to appear. As you stated earlier, I took office as attorney general back in January 1979, and within 6 months was forced to file suit against the Department of the Interior over 8(g) because of the refusal of the Secretary to make a fair and equitable offer for dividing Federal revenues.

As my term ended, we went to trial, and in the second year, and now the third year of my first term of Governor we are in the midst at the end of 7 years of a bitter litigation between the State and the Federal Government. I would hope to see it resolved by the action of this committee and Congress.

The Congress wisely recognizes it takes more than words to meet the goal of energy independence for this country and the hydrocarbon resources of OCS are believed by most knowledgeable oberverss to be an important part of the total domestic resource base.

The OCS can only be developed through a genuine spirit of Federal and State cooperation, and 8(g) land is apparently an appropriate way in which the Congress has decided to deal with the problem. Unfortunately, it was clear to everyone except the Department of the Interior. Time after time the Department has failed or refused to faithfully adhere to the congressional directives set out in the 1978 amendments.

Section 8(g) as written in 1978 sets out clear and unambiguous instructions to the Secretary, and with respect to the 8(g) zone, the Secretary was instructed by the statute to share both information and revenues as the revenues, bonus, royalty, and other revenues are to be shared fairly and equitably by agreement.

The problems we have discussed here today, basically the reason for the word "taxes" to be included in this was because of the way in which the Department of the Interior went about their leasing policy in Texas, and I have the commissioner of the State who is here, the former land commissioner in charge of our policy.

We set a sliding royalty on one tract of land that provides for royalty from 45 percent over a 3-year period up to a 55-percent royalty. The Department of the Interior went in and leased directly off that point based upon a royalty of one-sixth. Memorandums discovered in the litigation indicated this was a plan of operation on the part of the Department of the Interior to diminish those bonuses, to diminish royalties, and as a result, diminish the share, the fair and equitable share the States would receieve.

Therefore, in their memorandum they suggested they would pick it back up by virtue of taxes that would be received in the Treasury from the corporations who were developing that land offshore.

It appears many of those large oil companies have resolved that matter. Since many don't pay taxes, there is little claim there.

So, the reason for our suspicion was founded and well grounded in the evidence developed in the case before the court in Texas. That set about our State trying to make certain that there was going to be an appropriate leasing of those lands in order that there could be a fair and equitable division of the proceeds.

I think that has been pointed out dramatically here today in the testimony of the Secretary.

The focus that I would like to explain here is basically not to go into the complexities of this leasing policy, but to suggest that there are reasons for the policy. The State has impacts associated with the drilling off its coasts, and as Senator Bumpers suggested earlier, they won't get a penny out of this. The State of Texas has not gotten a penny out of this either.

As a result, if there had been some action taken by the Federal Government on the coast of Louisiana, in the sense that action taken in Missouri would impact Arkansas, then I would suggest that Arkansas would be entitled to some compensation by the Federal Government under this act.

This activity off the Outer Continental Shelf has an impact on the State. We have to provide for the economic activity that was generated. The schools, the roads, the infrastructure has to be built and maintained. Portions of this revenue are going directly for this purpose.

That is an impact direct and immediate on the State, and is an ongoing impact. It doesn't stop at the end of the bonus payment and the allocation of bonus. It is an ongoing impact that would necessarily follow a stream of revenue associated with royalty division. I think that, too, makes that royalty division appropriate.

The way in which the OCS has been developed by the Department of the Interior I think was incorrect when they started overlapping their tracts. I understand from testimony today that they will not in the future overlap tracts between 8(g) lands and the undisputed Federal ownership offshore, the Federal property land. I believe that will help solve that problem.

We are concerned about the escrow account and the suggestions that were made, and the court had ordered that all of the proceeds be deposited in escrow, and just as the statute had suggested.

However, an arbitrary decision on their part has apparently created a problem for this committee and the Congress, how to deal with the fact that they refuse to obey not only the clear meaning of the statute but the clear direction of the court over the deposit of those funds.

The injunction issued by Judge Parker was to prohibit any proration of those dollars. However, it appears the money was being withdrawn even while the Department was filing responses to our requests for injunction with the court.

After the Texas injunction was entered, the Department continued prorating across the country. That act was, I think, arrogant, but it is typical of the disdain with which the Department has viewed the mandate of the Congress and the judgment of the courts and the appropriate roles of the States.

In his letter quoting Judge Parker's opinion, again, typical of the Department's penchant for not quoting the full text, the Secretary quotes half of Judge Parker's footnote on proration. It is quite true that he held he could not directly give Texas money from that portion of the 8(g) tract outside the 8(g) zone, but the Secretary failed to tell you that in the next three sentences the judge ordered the Secretary to deposit all revenues from lease sales into escrow so that all revenues could be taken into account by the court in arriving at a fair and equitable division.

Senators Johnston and Murkowski have simply incorporated Judge Parker's mandate in this bill as the House Interior Committee has done. The recruitment portion is specifically designed to address the shortages in the escrow account to which I alluded earlier.

There is no question but that the States are required to share in moneys that the Secretary has wrongfully either withdrawn or failed to deposit. However, we understand that this Congress cannot make up that loss from current revenues, and that is why the States have agreed to be repaid out of future revenues at the rate of 10 percent per year. No other source would be used for that purpose.

We understand that permitting this current obligation to be paid with future dollars reduces to some extent the present value of the State's reimbursement, but we have not sought a larger State percentage to offset that benefit to the Federal Treasury. That is part of the compromise.

Another part of the Secretary's letter which is not only misleading but wrong deals with the alleged financial implications of S. 1653. I would not be surprised to learn that each of you has been contacted by either OMB or Interior and told that the financial sky is falling because of such a settlement.

The Secretary certainly tries to paint that picture in his letter by predicting that this bill will mean a $4 to $5 billion payment to the States from royalties over a 30-year period. I just wish that that were true. Unfortunately, we should all know better. After 7 years of leasing, there are barely $200 million in total 8(g) royalty payments in escrow.

The Congressional Budget Office projects royalty income of $100 million a year. If that forecast is correct, total 8(g) royalties for 30 years would only be $3 billion, and the State's share would be $810 million, a far cry from the $5 billion suggested by the Department.

Those of us who have dealt with the Department over the years are hardly surprised by their ability to creatively present facts. On the question of drainage, this is one of those areas. The Department has consistently contended that 8(g) was just to compensate a State for drainage.

We know that is not true. For one thing, two attempts were made during the original debate to make 8(g) specifically refer to drainage, but both of those amendments lost. Nowhere in 8(g) does the word "drainage" appear, and just as the Senator suggested, if they meant to divide it equally, why did they use the word "equitable."

If they meant to divide it based on drainage, why didn't they use the word "drainage," because they rejected that proposal. If drain-

age compensation were to go, States would logically share royalties but not bonuses or other revenues, and yet Congress required the Secretary to escrow not just production income royalties but bonuses and other revenues as well.

We later discovered that the Department also knew that 8(g) was not just a drainage statute because during the course of discovery we found a legal opinion dated December 1979, from the solicitor of the Department of the Interior.

In that memorandum the solicitor reviewed the legislative history of 8(g) and the statutory text, and concluded that the statute meant what it said. All revenues were subject to division. Nothing in the law permitted the Secretary to refuse to share bonuses or royalties, and his own lawyer told him so.

The fact is, for 7 years, four Secretaries of the Interior refused to share all 8(g) revenues, much less share them fairly and equitably. Even after we won the lawsuit, Secretary Clark's settlement offer refused to share Federal royalty income. Likewise, the administration's bill, which was defeated in the House Interior Committee, would refuse to share Federal royalty income.

The bill before the committee and the Huckaby substitute adopted by the House Interior Committee last week do give States a share of bonuses and royalties for both past and future lease sales. That is the major reason why we have been willing to support these bills.

As you know, I have aggressively sought a larger percentage than the 27-percent figure proposed. I have always believed that a fair and equitable division ought to be 50 percent just like the interim Mineral Leasing Act the States get.

As a compromise, five other Governors and I offered to settle for 37.5 percent, which was the States' share under the old Mineral Leasing Act before it was raised to 50 percent. That also represented a middle ground between the 50 percent of bonuses and royalties which the States wanted and the 16⅔ percent of the bonuses which Secretary Clark offered.

The Secretary's letter to you, Mr. Chairman, asserts that two courts have flatly rejected the claim that the States are entitled to 50 percent of the Federal revenue. His letter and other discussions have suggested the States would never get more than 27 percent because the 50 percent of bonus enhancement awarded by the Texas court equalled 27.5 percent of the revenues.

Again, the Secretary, I think, is wrong. He misunderstood the status of the litigation in the first place. Neither Texas nor Louisiana courts have been asked to rule on a flat 50 percent. Because of the nature of the issues, the issues are not proposed that way. Only Texas has had a trial on the merits, and the only thing litigated in Texas has been the division of bonuses from tracts in four lease sales.

If this statute is not passed, and the litigation continues, numerous other State claims will remain to be heard. For example, no decision has been made about the State's share of royalties. Moreover, we learned in discovery that the Department receives about one-third of its income from these leases in the form of taxes.

We further learned that one reason the Department has held royalties low is because it believes that lower royalties shift reve-

nues into taxes, and while this Department feared it might have to share bonuses and royalties, it did not expect to share taxes.

On deposition Department personnel testified they did not think the States would be smart enough to figure this out. Judge Parker has agreed to hear evidence on the tax and has ruled that if certain standards are met, tax revenues are subject to division. The Louisiana court has agreed with Judge Parker, and will also hear evidence on point.

Judge Parker has also indicated he would hear evidence on the huge decline in bonus receipts which occurred when the Department began its areawide leasing program. That would also be a factor relevant to a fair and equitable division. All of this simply says that the Secretary was wrong to imply that the States had no opportunity to win more than 27 percent of total revenues.

However, in spite of the success which we have enjoyed in the courthouse, my fellow Governors and I do not favor continuing the litigation. It has been 7 years since the Congress adopted this section and not a single dollar of these Federal revenues has been shared with the States. Nothing about that is either fair or equitable.

Neither is it appropriate to force the States into decades of litigation, which is very expensive. This issue needs to be settled fairly, and I trust the Congress will. Certainly the States feel entitled to more than 27 percent. The reality of the budget's crisis does not exist just at the Federal level, however, and I understand very well we are here today because the Federal Government needs and is taking $4 billion out of the 8(g) escrow account.

I appreciate the Federal need for these revenues, but the States need their fair share as well, and their needs are just as real, as those of you who have been Governors of your States no doubt recall.

I would at this time conclude my remarks, and try to respond to any questions members of the committee might have.

[The prepared statement of Governor White follows:]

TESTIMONY OF THE HONORABLE MARK WHITE, GOVERNOR OF TEXAS

CHAIRMAN MCCLURE AND DISTINGUISHED MEMBERS OF THE SENATE ENERGY AND NATURAL RESOURCES COMMITTEE:

I APPRECIATE YOUR INVITATION TO APPEAR BEFORE YOU TODAY TO DISCUSS S. 1653, SPONSORED BY SENATORS JOHNSTON AND MURKOWSKI AND WHICH I AM HERE TO SUPPORT, AS WELL AS THE 8(G) ISSUE GENERALLY.

I TOOK OFFICE AS ATTORNEY GENERAL OF TEXAS IN JANUARY OF 1979. WITHIN SIX MONTHS, I WAS FORCED TO FILE SUIT AGAINST THE DEPARTMENT OF INTERIOR OVER 8(G) BECAUSE THE SECRETARY REFUSED TO MAKE A FAIR AND EQUITABLE OFFER FOR DIVIDING FEDERAL REVENUES. AS MY TERM ENDED FOUR YEARS LATER, THAT CASE WENT TO TRIAL. IN THE SECOND YEAR OF MY TERM AS GOVERNOR, THE COURT ANNOUNCED THAT WE HAD WON. NOW, AS THE THIRD YEAR OF MY FIRST TERM AS GOVERNOR DRAWS NEAR, WE HAVE AN OPPORTUNITY TO END SEVEN YEARS OF BITTER LITIGATION BETWEEN THE STATES AND THE FEDERAL GOVERNMENT. THE NATIONAL INTEREST REQUIRES THAT IT BE DONE.

IN 1978 THE CONGRESS WISELY RECOGNIZED THAT IT TAKES MORE THAN WORDS TO MEET THE GOAL OF ENERGY INDEPENDENCE FOR THIS COUNTRY. THE HYDROCARBON RESOURCES OF THE OCS ARE BELIEVED BY MOST KNOWLEDGEABLE OBSERVERS TO BE AN IMPORTANT PART OF A TOTAL DOMESTIC RESOURCE BASE WHICH CAN BE DEVELOPED TO INSURE THAT OUR NATIONAL SECURITY IS NOT JEOPARDIZED BY AN UNWISE AND EXCESSIVE DEPENDENCE ON FOREIGN OIL AND GAS SUPPLIES. THE OCS CAN ONLY BE DEVELOPED EFFECTIVELY THROUGH A GENUINE SPIRIT OF FEDERAL-STATE COOPERATION. WHEN CONGRESS WROTE THE 1978 OUTER CONTINENTAL SHELF LANDS ACT AMENDMENTS IN WHICH SECTION

8(G) APPEARED. CONGRESS OBVIOUSLY THOUGHT IT WAS DRAFTING A FRAMEWORK FOR COOPERATION BETWEEN THE STATES AND THE FEDERAL GOVERNMENT WHICH WOULD FACILITATE THE PROMPT AND EFFICIENT DEVELOPMENT OF THE OIL AND GAS RESOURCES OF THE OCS. THE FRAMEWORK AND THE WORDS WHICH CONGRESS CHOSE TO IMPLEMENT OCS LEASING THROUGH THE 1978 AMENDMENTS MAKE IT ABSOLUTELY CLEAR THAT CONGRESS BELIEVED THAT COOPERATION AND MEANINGFUL CONSULTATION WITH THE COASTAL STATES WAS ESSENTIAL TO A SUCCESSFUL FEDERAL OCS LEASING PROGRAM.

UNFORTUNATELY, IT WAS CLEAR TO EVERYONE EXCEPT THE DEPARTMENT OF INTERIOR. TIME AFTER TIME, THE DEPARTMENT HAS FAILED OR REFUSED TO FAITHFULLY ADHERE TO THE CONGRESSIONAL DIRECTIVES SET OUT IN THE 1978 AMENDMENTS. SECTION 8(G) IS ONE SUCH EXAMPLE, AND THAT IS WHY WE ARE HERE THIS MORNING.

SECTION 8(G), AS WRITTEN IN 1978, SETS OUT CLEAR AND UNAMBIGUOUS INSTRUCTIONS TO THE SECRETARY OF THE INTERIOR WITH RESPECT TO THE LEASING OF FEDERAL TRACTS WITHIN A THREE MILE ZONE ADJACENT TO STATE SUBMERGED LANDS. THIS AREA, WHICH HAS BECOME KNOWN AS THE 8(G) ZONE, IS SIMPLY A THREE MILE WIDE BELT OF FEDERAL SUBMERGED LANDS WHICH RUNS PARALLEL AND ADJACENT TO STATE SUBMERGED LANDS. WITH RESPECT TO THIS 8(G) ZONE, THE SECRETARY IS INSTRUCTED BY THE STATUTE TO SHARE BOTH INFORMATION AND REVENUES. AS TO THE REVENUES, "BONUS, ROYALTY AND OTHER REVENUES ARE TO BE SHARED FAIRLY AND EQUITABLY BY AGREEMENT BETWEEN THE SECRETARY AND GOVERNOR OR BY A FEDERAL DISTRICT COURT IF NO AGREEMENT IS REACHED.

CONGRESS ADDED SECTION 8(G) TO THE 1978 AMENDMENTS AS PART OF THE RECOGNITION THAT COASTAL STATES WHICH ARE ADJACENT TO FEDERAL OCS LEASING BEAR SPECIAL RISKS AND BURDENS ON BEHALF OF THEIR SISTER STATES. OBVIOUSLY, CONGRESS BELIEVED THAT THE REVENUE DIVISION COULD BE HANDLED AMICABLY BY RATIONAL INDIVIDUALS. UNFORTUNATELY, WHAT CONGRESS FAILED TO FORESEE WAS THAT THE DEPARTMENT'S IDEA OF A FAIR AND EQUITABLE DIVISION WAS FOR THEM TO GET ALL OF THE MONEY.

FROM THE DAY THE STATUTE BECAME LAW, THE SECRETARY HAS RESISTED SHARING EITHER INFORMATION OR REVENUES. THE FACT THAT WE ARE HERE TODAY IN THE CONTEXT OF THE BUDGET RECONCILIATION PROCESS, HOWEVER, MAKES IT DIFFICULT TO DENY THAT IT IS THE DIVISION OF REVENUES WHICH IS OF PRIMARY CONCERN TO BOTH THE STATES AND THE FEDERAL GOVERNMENT.

IN MY TESTIMONY THIS MORNING I WANT TO FOCUS ON A FEW OF THE MANY ISSUES INVOLVED IN THIS 8(G) COTROVERSY AND I WANT TO TRY TO EXPLAIN WHY THE STATES ARE WILLING TO ACCEPT SENATORS JOHNSTON AND MURKOWSKI'S PROPOSED SOLUTION. I DO NOT PROPOSE TO RECOUNT ALL OF THE COMPLEXITIES OF THE ISSUES OR ALL OF THE DISPUTES WHICH WE HAVE HAD WITH THE DEPARTMENT BECAUSE I UNDERSTAND THAT WE NEED TO FINISH THIS MORNING.

ALTHOUGH I WAS NOT PRESENT AT YOUR MARKUP SESSION LAST FRIDAY, I HAVE HAD THE OPPORTUNITY TO READ THE LETTER SECRETARY HODEL SENT TO THE COMMITTEE. I UNDERSTAND THAT SEVERAL QUESTIONS WERE RAISED AS A RESULT OF HIS LETTER. BECAUSE THE SECRETARY'S LETTER IS MISLEADING,

AND IN PLACES SIMPLY INCORRECT, IT IS VERY IMPORTANT FOR THE COMMITTEE TO HAVE THE BENEFIT OF THE PERSPECTIVE OF THE STATES ON THOSE ISSUES.

I WANT TO BEGIN WITH TWO ISSUES WHICH ARE CLOSELY LINKED - FIRST, THE DEPARTMENT'S PRACTICE OF PRORATING LEASE REVENUES AND SECOND, WHAT S. 1653 REFERS TO AS RECOUPMENT.

AS YOU KNOW, THE INTERIOR DEPARTMENT HAS COMPLETE DISCRETION OVER THE SIZE OF THE FEDERAL OCS TRACTS WHICH IT OFFERS FOR LEASE. THE DEPARTMENT DECIDES HOW AND WHERE TRACT BOUNDARIES SHOULD BE DRAWN. IN THE FIRST FEW YEARS, AFTER SECTION 8(G) BECAME EFFECTIVE, THE DEPARTMENT DREW SOME TRACT BOUNDARIES SO THAT THOSE TRACTS WERE PARTIALLY WITHIN AND PARTIALLY BEYOND THE 8(G) ZONE. WHILE PREPARING FOR OUR TRIAL, WE DISCOVERED SOME INTERNAL DEPARTMENT OF INTERIOR MEMORANDA IN WHICH THE VARIOUS ASSISTANT SECRETARIES WHO WERE INVOLVED IN OCS LEASING SPECIFICALLY DISCUSSED WHETHER THESE TRACTS SHOULD BE PERMITTED TO OVERLAP THE 8(G) ZONE OR WHETHER THEY SHOULD DRAW THE TRACTS TO BE COTERMINUS WITH THE 8(G) BOUNDARY. BY CONSCIOUS DECISION, THE DEPARTMENT CHOSE TO PERMIT THE TRACTS TO OVERLAP.

DURING THE EARLY YEARS, IT APPEARS THAT THE DEPARTMENT DEPOSITED INTO ESCROW ALL OF THE BONUS, RENT AND ROYALTY INCOME FROM THESE OVERLAP TRACTS JUST LIKE THE STATUTE SAID TO DO. IN 1982, HOWEVER, AS BUDGET PRESSURES FROM OMB BEGAN TO GROW, THE DEPARTMENT ANNOUNCED THAT IT INTENDED (A) TO PRORATE THE LEASE REVENUES ON A SURFACE ACREAGE BASIS AND (B) TO WITHDRAW FROM ESCROW THOSE FUNDS ATTRIBUTABLE TO PORTIONS OF THE OVERLAP TRACTS WHICH WERE BEYOND THE 8(G) ZONE.

WHEN WE WERE NOTIFIED OF THAT INTENTION, WE WENT TO JUDGE PARKER AND SOUGHT AN INJUNCTION DIRECTING THE DEPARTMENT TO LEAVE THE MONEY IN ESCROW. JUDGE PARKER ISSUED THAT INJUNCTION AND PROHIBITED PRORATIONS. HOWEVER, IT NOW APPEARS THAT THE MONEY WAS BEING WITHDRAWN EVEN WHILE THE DEPARTMENT WAS FILING RESPONSES TO OUR REQUEST FOR INJUNCTION WITH THE COURT. AFTER THE TEXAS INJUNCTION WAS ENTERED, THE DEPARTMENT CONTINUED ITS PRORATIONING ACROSS THE COUNTRY. THAT ACT OF ARROGANCE IS TYPICAL OF THE DISTAIN WITH WHICH THE DEPARTMENT HAS VIEWED THE MANDATE OF CONGRESS, THE JUDGMENT OF THE COURTS, AND THE ROLE OF THE STATES.

IN HIS LETTER TO YOU, MR. CHAIRMAN, THE SECRETARY ATTEMPTS TO JUSTIFY HIS PRORATIONING PRACTICE BY QUOTING JUDGE PARKER IN THE TEXAS OPINION. AGAIN, TYPICAL OF THE DEPARTMENT'S PENCHANT FOR HALF-TRUTHS, THE SECRETARY ONLY QUOTES HALF OF JUDGE PARKER'S FOOTNOTE ON PRORATIONING. IT IS QUITE TRUE THAT JUDGE PARKER HELD THAT HE COULD NOT DIRECTLY GIVE TEXAS MONEY FROM THAT PORTION OF A TRACT BEYOND THE 8(G) ZONE. WHAT THE SECRETARY FAILED TO TELL YOU IS THAT IN THE NEXT THREE SENTENCES, JUDGE PARKER ORDERED THE SECRETARY TO DEPOSIT ALL REVENUES FROM LEASE SALES INTO ESCROW SO THAT ALL REVENUES COULD BE TAKEN INTO ACCOUNT BY THE COURT IN ARRIVING AT A FAIR AND EQUITABLE DIVISION. JUDGE PARKER OBSERVED THAT MAKING THAT DIVISION WAS THE COURT'S JOB ABSENT AGREEMENT. PRORATIONING PERMITS THE SECRETARY TO UNILATERALLY DECIDE HOW MUCH MONEY WILL BE DIVIDED. JUDGE PARKER REJECTED THAT. THE COURT THEN POINTED OUT THAT THE SECRETARY COULD AVOID THIS PROBLEM ALL TOGETHER BY THE WAY HE DREW THE TRACT LINES.

SENATORS JOHNSTON AND MURKOWSKI HAVE SIMPLY INCORPORATED JUDGE PARKER'S MANDATE IN THIS BILL, AS THE HOUSE INTERIOR COMMITTEE HAS DONE.

THE RECOUPMENT PORTION OF S. 1653 IS SPECIFICALLY DESIGNED TO ADDRESS THE SHORTAGES IN THE ESCROW ACCOUNT WHICH HAVE RESULTED FROM THE DEPARTMENT'S PRORATION POLICY. PERSONALLY, I BELIEVE RESTITUTION IS AS DESCRIPTIVE A WORD AS RECOUPMENT.

AS I INDICATED EARLIER, IT APPEARS THAT THE DEPARTMENT HAS WITHDRAWN SOME TEXAS FUNDS FROM THE ACCOUNT. WE KNOW THAT MONIES HAVE BEEN WITHHELD FROM ALL OTHER STATES AS WELL, BUT IT IS IMPOSSIBLE TO TELL YOU ACCURATELY THIS MORNING JUST HOW MUCH THAT IS BECAUSE THE ESCROW ACCOUNT HAS BEEN MANAGED SO INEPTLY AS THE DIRECTOR OF THE MINERALS MANAGEMENT SERVICE ADMITTED BEFORE THE HOUSE INTERIOR COMMITTEE ON JULY 29TH OF THIS YEAR. WITHOUT AN INDEPENDENT AUDIT, IT IS NOT POSSIBLE TO KNOW WITH CONFIDENCE WHAT THE TRUE CONDITION OF THE ACCOUNT IS OR WHAT IT SHOULD BE.

THERE IS NO QUESTION BUT THAT THE STATES ARE ENTITLED TO SHARE IN MONIES WHICH THE SECRETARY WRONGLY EITHER WITHDREW OR FAILED TO DEPOSIT. HOWEVER, WE UNDERSTAND THAT THIS CONGRESS CANNOT MAKE-UP THAT LOSS FROM CURRENT REVENUES. THAT IS WHY THE STATES HAVE AGREED TO BE REPAID OUT OF FUTURE 8(G) REVENUES AT THE RATE OF 10% A YEAR. NO OTHER REVENUE SOURCE WILL BE USED FOR THAT PURPOSE. WE CERTAINLY UNDERSTAND THAT PERMITTING THIS CURRENT OBLIGATION TO BE PAID WITH FUTURE DOLLARS REDUCES TO SOME EXTENT THE PRESENT VALUE OF THE STATES'

REIMBURSEMENT, BUT WE HAVE NOT SOUGHT A LARGER STATE PERCENTAGE TO OFFSET THAT BENEFIT TO THE FEDERAL TREASURY. THAT IS PART OF OUR COMPROMISE.

ANOTHER PART OF THE SECRETARY'S LETTER WHICH IS NOT ONLY MISLEADING BUT JUST WRONG DEALS WITH THE ALLEGED FINANCIAL IMPLICATIONS OF S. 1653. I WOULD NOT BE SURPRISED TO LEARN THAT EACH OF YOU HAVE BEEN CONTACTED BY EITHER OMB OR INTERIOR AND TOLD THAT THE FINANCIAL SKY IS FALLING BECAUSE OF THIS 8(G) SETTLEMENT. THE SECRETARY CERTAINLY TRIES TO PAINT THAT PICTURE IN HIS LETTER BY PREDICTING THAT THIS BILL WILL MEAN A $4-5 BILLION PAYMENT TO THE STATES FROM ROYALTIES OVER A THIRTY YEAR PERIOD.

I JUST WISH THAT WERE TRUE. UNFORTUNATELY, I KNOW BETTER. AFTER SEVEN YEARS OF LEASING, THERE ARE BARELY $200 MILLION IN TOTAL 8(G) ROYALTY PAYMENTS IN ESCROW. THE CONGRESSIONAL BUDGET OFFICE PROJECTS ROYALTY INCOME OF $100 MILLION A YEAR. IF THAT FORECAST IS CORRECT, <u>TOTAL</u> 8(G) ROYALTIES FOR 30 YEARS WOULD BE ONLY $3 BILLION AND THE STATE SHARE WOULD BE $810 MILLION, HARDLY CLOSE TO $5 BILLION.

OF COURSE, THOSE OF US WHO HAVE DEALT WITH THE DEPARTMENT ON 8(G) OVER THE LAST YEARS ARE HARDLY SURPRISED BY THEIR ABILITY TO CREATIVELY PRESENT THE FACTS. TAKE, FOR EXAMPLE, THE SECRETARY'S REFERENCE TO DRAINAGE.

THE DEPARTMENT HAS CONSISTENTLY MAINTAINED TO TEXAS THAT SECTION 8(G) WAS JUST INTENDED TO COMPENSATE A STATE FOR DRAINAGE OF A STATE'S OIL AND GAS BY A FEDERAL LESSEE.

NOW WE KNEW THAT WAS NOT TRUE. FOR ONE THING, TWO ATTEMPTS WERE MADE DURING THE ORIGINAL CONGRESSIONAL DEBATE TO MAKE 8(G) SPECIFICALLY REFER TO DRAINAGE. BOTH AMENDMENTS LOST. NO WHERE IN 8(G) DOES THE WORD DRAINAGE APPEAR. FOR ANOTHER THING, IF DRAINAGE COMPENSATION WERE THE GOAL, STATES WOULD LOGICALLY SHARE ROYALTIES BUT NOT BONUS OR OTHER REVENUES. YET, CONGRESS REQUIRED THE SECRETARY TO ESCROW NOT JUST PRODUCTION INCOME ROYALTIES - BUT BONUSES AND OTHER REVENUES AS WELL.

WE LATER DISCOVERED THAT THE DEPARTMENT ALSO KNEW THAT 8(G) WAS NOT JUST A DRAINAGE STATUTE. DURING THE COURSE OF DISCOVERY, WE FOUND A LEGAL OPINION DATED DECEMBER 1979 FROM THE SOLICITOR OF THE DEPARTMENT OF INTERIOR. IN THAT MEMORANDUM, THE SOLICITOR REVIEWED THE LEGISLATIVE HISTORY OF 8(G) AND THE STATUATORY TEXT AND CONCLUDED THAT THE STATUTE MEANT WHAT IT SAID; ALL REVENUES WERE SUBJECT TO DIVISION. NOTHING IN THE LAW PERMITTED THE SECRETARY TO REFUSE TO SHARE BONUSES OR ROYALTIES, AND HIS OWN LAWYER TOLD HIM SO.

BUT THE FACT IS THAT FOR SEVEN YEARS FOUR SECRETARIES OF THE INTERIOR HAVE REFUSED TO SHARE ALL 8(G) REVENUES, MUCH LESS SHARE THEM FAIRLY AND EQUITABLY. EVEN AFTER WE WON THE LAWSUIT, SECRETARY CLARK'S SETTLEMENT OFFER REFUSED TO SHARE FEDERAL ROYALTY INCOME.

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LIKEWISE, THE ADMINISTRATION'S BILL WHICH WAS DEFEATED IN THE HOUSE INTERIOR COMMITTEE WOULD HAVE REFUSED TO SHARE FEDERAL ROYALTY INCOME.

BOTH THE JOHNSTON-MURKOWSKI BILL WHICH IS BEFORE YOU TODAY AND THE HUCKABY SUBSTITUTE ADOPTED BY THE HOUSE INTERIOR COMMITTEE LAST WEEK DO GIVE THE STATES A SHARE OF BONUSES AND ROYALTIES FOR BOTH PAST AND FUTURE LEASE SALES. THAT IS A MAJOR REASON WHY WE HAVE BEEN WILLING TO SUPPORT THESE BILLS.

AS YOU KNOW, I HAVE AGGRESSIVELY SOUGHT A LARGER PERCENTAGE THAN THE 27% FIGURE WHICH IS PROPOSED. I HAVE ALWAYS BELIEVED THAT A FAIR AND EQUITABLE DIVISION OUGHT TO BE 50%, JUST LIKE THE INLAND MINERAL LEASING ACT STATES GET. AS A COMPROMISE, FIVE OTHER GOVERNORS AND I OFFERED TO SETTLE FOR 37 1/2% WHICH WAS THE STATE SHARE UNDER THE OLD MINERAL LEASING ACT BEFORE IT WAS RAISED TO 50%. THAT ALSO REPRESENTED THE MIDDLE GROUND BETWEEN THE 50% OF BONUSES AND ROYALTIES WHICH THE STATES WANTED AND THE 16 2/3% OF BONUSES WHICH SECRETARY CLARK OFFERED.

THE SECRETARY'S LETTER TO YOU, MR. CHAIRMAN, ASSERTS THAT TWO COURTS HAVE "FLATLY REJECTED" THE CLAIM THAT THE STATES ARE ENTITLED TO 50% OF THE FEDERAL 8(G) REVENUES. HIS LETTER AND OTHER DISCUSSION HAVE SUGGESTED THAT THE STATES WOULD NEVER GET MORE THAN 27% BECAUSE THE 50% OF BONUS ENHANCEMENT AWARDED BY THE TEXAS COURT EQUALLED 27% OF THE TOTAL REVENUES.

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AGAIN, THE SECRETARY IS SIMPLY WRONG. HE MISUNDERSTANDS THE STATUS OF THE LITIGATION.

IN THE FIRST PLACE, NEITHER THE TEXAS NOR THE LOUISIANA COURTS HAVE BEEN ASKED TO RULE ON A FLAT 50% DIVISION. BECAUSE OF THE NATURE OF THE LITIGATION, THE ISSUES SIMPLY ARE NOT POSED THAT WAY.

ONLY TEXAS HAS HAD A TRIAL ON THE MERITS OF ANY OF THE 8(G) ISSUES, AND THE ONLY THING WHICH HAS BEEN LITIGATED IN TEXAS IS THE DIVISION OF BONUSES FROM TRACTS IN FOUR LEASE SALES.

IF THIS STATUTE IS NOT PASSED AND THE LITIGATION CONTINUES, NUMEROUS OTHER STATE CLAIMS REMAIN TO BE HEARD. FOR EXAMPLE, NO DECISION HAS BEEN MADE ABOUT THE STATE'S SHARE OF ROYALTIES. MOREOVER, WE LEARNED IN DISCOVERY THAT THE DEPARTMENT RECEIVES ABOUT ONE THIRD OF ITS INCOME FROM THESE LEASES IN THE FORM OF TAXES. WE FURTHER LEARNED THAT ONE REASON THE DEPARTMENT HAS HELD ROYALTIES LOW IS BECAUSE IT BELIEVES THAT LOWER ROYALTIES SHIFT REVENUE INTO TAXES, AND WHILE THE DEPARTMENT FEARED IT MIGHT HAVE TO SHARE BONUSES AND ROYALTIES WITH THE STATES, IT DID NOT EXPECT TO SHARE TAXES. ON DEPOSITION, DEPARTMENT PERSONNEL TESTIFIED THAT THEY DID NOT THINK THAT THE STATES WOULD BE SMART ENOUGH TO FIGURE THIS OUT.

JUDGE PARKER HAS AGREED TO HEAR EVIDENCE ON THE TAX ISSUE AND HAS RULED THAT, IF CERTAIN STANDARDS ARE MET, TAX REVENUES ARE SUBJECT TO DIVISION. THE LOUISIANA COURT HAS AGREED WITH JUDGE PARKER AND WILL ALSO HEAR EVIDENCE ON THIS POINT.

JUDGE PARKER HAS ALSO INDICATED THAT HE WOULD HEAR EVIDENCE ON THE HUGE DECLINE IN BONUS RECEIPTS WHICH OCCURRED WHEN THE DEPARTMENT BEGAN ITS AREA WIDE LEASING PROGRAM. THAT ALSO WOULD BE A FACTOR RELEVANT TO A FAIR AND EQUITABLE DIVISION.

ALL OF THIS IS SIMPLY TO SAY THAT THE SECRETARY IS WRONG TO IMPLY THAT THE STATES HAVE NO OPPORTUNITY TO WIN MORE THAN 27% OF TOTAL REVENUES. HOWEVER, IN SPITE OF THE SUCCESS WHICH WE HAVE ENJOYED IN THE COURTHOUSE, MY FELLOW GOVERNORS AND I DO NOT FAVOR CONTINUING THE LITIGATION.

IT HAS BEEN SEVEN YEARS SINCE CONGRESS ADOPTED SECTION 8(G) AND NOT A SINGLE DOLLAR OF THESE FEDERAL REVENUES HAS BEEN SHARED WITH THE STATES. NOTHING ABOUT THAT IS EITHER FAIR OR EQUITABLE. NEITHER IS IT APPROPRIATE TO FORCE THE STATES INTO DECADES OF EXPENSIVE LITIGATION BEFORE THEY OBTAIN THAT FAIR SHARE.

THIS ISSUE NEEDS TO BE SETTLED FAIRLY. SINCE THE SECRETARY WILL NOT, THE CONGRESS MUST.

CERTAINLY, THE STATES FEEL THEY ARE ENTITLED TO MORE THAN 27%. THE REALITY OF BUDGET CRISIS DOES NOT EXIST JUST AT THE FEDERAL LEVEL, HOWEVER. I UNDERSTAND VERY WELL THAT WE ARE HERE TODAY BECAUSE THE FEDERAL GOVERNMENT NEEDS - AND IS TAKING - $4 BILLION OUT OF THE 8(G) ESCROW ACCOUNT. I APPRECIATE THE FEDERAL NEED FOR THOSE REVENUES, BUT THE STATES NEED THEIR FAIR SHARE AS WELL AND THE NEED IS JUST

AS REAL, AS THOSE OF YOU WHO HAVE BEEN GOVERNOR OF YOUR STATE NO DOUBT RECALL VERY VIVIDLY.

THE DEVELOPMENT OF AMERICA'S ENERGY RESOURCES OUGHT TO BE A COOPERATIVE EFFORT BETWEEN THE STATES AND THE FEDERAL GOVERNMENTS. CONGRESS PLAINLY SENT THAT MESSAGE IN 1978; UNFORTUNATELY THE DEPARTMENT HAD DIFFERENT IDEAS AND SEVEN YEARS OF LITIGATION HAVE FOLLOWED.

THE ISSUE NEEDS TO BE SETTLED. THIS IS THE ONLY CASE I HAVE EVER BEEN INVOLVED IN WHERE THE JUDGE FOUND AS A MATTER OF FACT THAT THE CASE WAS SO COMPLICATED THAT CONGRESS NEEDED TO CHANGE THE LAW. TODAY, THE COUNTRY NEEDS YOU TO CLOSE THIS DEBATE BY ADOPTING THE JOHNSTON-MURKOWSKI PROPOSAL. HOPEFULLY, WE CAN THEN TURN MORE ATTENTION TO THE REAL TASK WHICH IS THE ASSURANCE OF ENERGY INDEPENDENCE AND OUR NATIONAL SECURITY.

Senator MURKOWSKI. Thank you very much, Governor.

I am wondering if you would care to comment on the Secretary's contention that only 1 to 4 percent of oils come from common pools.

Governor WHITE. The use of the word "common pools" does not have a great deal of relevance today, I think, in the development of——

Senator MURKOWSKI. So you don't necessarily agree, or your geologist wouldn't necessarily agree with the generalization of the Secretary.

Governor WHITE. I think the word "common pools" indicates that somewhere below the surface of the Earth there is a volume of liquid in a pool form, and it is easily discerned exactly the termination point of that pool. That simply is not realistic.

Senator MURKOWSKI. What do you think is realistic?

Governor WHITE. It is a much more sophisticated determination than that, and frankly the only way you can ever determine what a reservoir would be, would be after it was developed. In other words you have to drill it all the way out, and it may take you 20 years.

In fact, there is continued drilling in the old east Texas field, and they still expand and shift the limits of that field, so there is very little way to resolve it on the basis of drainage, because you will never know until after you have developed the total reservoir where that reservoir exists, and you may never determine it in our lifetime and maybe for generations to come.

Senator MURKOWSKI. If it is significantly higher, the contention of the Secretary or his geologists, what conclusion do you draw from that statement, that only 1 to 4 percent?

Governor WHITE. I think it is false, and I don't think there is any basis for it, and I think you will find that that is just a guess that will be as wrong as the other guesses these people have made about the whole matter of leasing that they have been operating under.

Senator MURKOWSKI. Do you have any feeling with regard to the statement that once geological data is known, that it is possible to determine if common pools exist?

Governor WHITE. Probably one of the best developed fields in Texas, the Panhandle field, runs all the way up into Kansas. That was discovered in the late twenties. They are still arguing today in FERC over what the reservoir limits are in that field. You are talking 60 years, and they are arguing about whether gas is produced at one level of the field and oil at another. I would think the proposal suggested here is unworkable.

Senator MURKOWSKI. Do you or your State department of geology have any factual information that would substantiate the position that little or no drainage occurs from State lands, or can you provide us with data that indicates that there is substantial drainage from State lands?

Governor WHITE. The Department of the Interior will not share that information.

Senator MURKOWSKI. How about your own State information that your geologists have?

Governor WHITE. I believe that is proprietary information.

Senator MURKOWSKI. You might check on it, because it is the position that the Secretary of the Interior has taken that little or no drainage occurs from State lands, and the committee would appreciate any information to the contrary if it can be determined for public consumption.

Governor WHITE. There has been relatively little development at this time, so there is drainage where it comes across our land, but on the drainage theory, we should be compensated 100 percent for drainage. I mean, that is not an argument of 27 percent. They get 73 percent of something when they weren't entitled to anything.

Senator MURKOWSKI. But the Secretary's contention is, it isn't an issue because it doesn't happen, and my point is, if we can get some information that indeed there is some exposure, you have evidence that it does flow from State to Federal.

Governor WHITE. Let me say it would be the first time in the history of the industry that you didn't have drainage under those circumstances. It would be a new find on the part of the Secretary.

Senator MURKOWSKI. We appreciate your testimony.

Senator Johnston.

Senator JOHNSTON. Thank you very much, Governor, for your excellent testimony.

Governor, were you attorney general when this decision on the *State of Texas* v. *the Secretary of the Interior*, this decision was rendered?

Governor WHITE. No, sir, I was Governor at that time. I was attorney general when we filed the case.

Senator JOHNSTON. There is this footnote which has been discussed here. Now, is it not true that in that footnote the judge says first that he has no jurisdiction beyond the 8(g) zone. Second, with respect to existing leases, that he has divided the revenue that he has put into the pot, which was later divided 50-50 on enhanced bonuses, all of the lease, including that which was outside the 8(g) zone?

Governor WHITE. Yes, sir. He intended, I believe, by his statement here to include everything that was flowing or any revenue stream from the 8(g) tract.

Senator JOHNSTON. And for future leases, he recommends to the Government, and they have since adopted that policy, that he lease only up to the line—I mean that they lease only up to the line.

Governor WHITE. Yes.

Senator JOHNSTON. So in effect, what the judge did by saying he had no jurisdiction there, he included the whole lease, even beyond the 8(g) zone for the purposes of determining what was fair and equitable.

Governor WHITE. Yes, sir. Precisely.

Senator JOHNSTON. I think that is very important here because it seems to me that is the crux of this matter. The judge that included that, when the judge made his decision, he included the whole tract, including that which was beyond the 8(g) zone.

Now, Governor, you refer in your letter to a Department of the Interior solicitor's opinion which adopts the same view. I think that was back in 1980.

Governor WHITE. September 27, 1979.

Senator JOHNSTON. The Department's own solicitor stated or had an opinion which in effect said, you put the whole tract in. Am I correct?

Governor WHITE. Yes, sir.

Senator JOHNSTON. You refer to that chapter and verse in your statement.

Governor WHITE. The reference I was making was that all of the revenue should be taken into account on the division.

Senator JOHNSTON. Well, is it correct that the Department of the Interior, in its own policy from the passage of this bill in 1978, until Mr. Watt made a decision in 1981, included all revenues without prorationing?

Governor WHITE. That's correct.

Senator JOHNSTON. And are you familiar with a Department of the Interior solicitor's opinion—the date of that is—it is 1979. I have a copy of it which supports that.

Governor WHITE. Yes, sir; there is. It's not the one I mentioned by date here, but there is another solicitor's opinion about the deposit of those funds.

Senator JOHNSTON. And when the Department of the Interior came out with the initial figures that decided how much would go to each State, they were based upon all of the tracts prior to 1981 not being prorationed, were they not?

Secretary HODEL. Yes, sir.

Senator JOHNSTON. So when the Secretary of the Interior said that no one ever believed that you should have no prorationing, and when it is absolutely clear under the statute he is going contrary to a solicitor, contrary to the policy of the Department of the Interior, contrary to every court that has ever ruled on this question, and this new-found knowledge which is so clear has been in existence only in latter years; is that not so?

Governor WHITE. That's exactly correct. And I think the reason for that, among others, is they can artfully draw those tracts to divert and change the results, just the way they draw the lines.

They could have a tract that ran very narrowly down, and a strip annexation approach to it, and pick a well up down here and then balloon the tract out on the other side of the 8(g) line, and then prorate it on an acreage basis. And that tract would obviously be much more in the Federal site than the——

Senator JOHNSTON. Surface acreage doesn't have a great deal to do with it.

Governor WHITE. It has nothing to do with it. It would be a promotion of fraud to allow them to do that.

Senator JOHNSTON. Governor, we also have a provision of this bill called recoupment, and the recoupment is based upon there being a consistent policy on the proration issue, is it not?

Governor WHITE. Yes, sir.

Senator JOHNSTON. These moneys paid into the fund, I think it's clear to all of the members of this committee, those were real moneys, that $5.8 billion. I mean that's real hard cash paid into a fund somewhere and if it no longer exists, it's not the fault of the State that it no longer exists.

Governor WHITE. Absolutely.

Senator JOHNSTON. Governor, you are familiar with—I don't know whether Texas has done this, but even prior to 1978 I know in the State of Louisiana, they provided for unitization. Are you familiar with that policy of Louisiana? I know that there were 144 different Federal/State units, unitization agreements in place in offshore Louisiana as of 1978.

Are you familiar with that?

Governor WHITE. Yes.

Senator JOHNSTON. I really wanted to ask this to the Secretary of the Interior because he said this whole statute was for the purpose of dealing with the problem of drainage and unitization is the classic way of dealing with drainage, is it not?

Governor WHITE. Yes, sir.

Senator JOHNSTON. And so, here this committee goes through the legislative process in drafting a statute providing for fair and equitable resolution, and the Secretary of the Interior says it's only for drainage, when actually we had a policy predating this by a long time, dealing with drainage.

Governor WHITE. Yes, sir.

Senator JOHNSTON. Now, Governor, just one more word. I don't know whether you are familiar with all of the legislative history that predated this matter. This amendment really began in this committee.

The Secretary said it began with a letter from Representative Miller in the House. Actually, it began in this committee. I provided the only amendment to that, as I recall, on a question of partial distribution of the revenues. But the amendment came about because in the—I promise you, I have a piece of paper here—this legislation began on March 22, 1974, when Senator Jackson introduced S. 521 which was virtually identical to S. 3221.

And S. 3221 wound its way through the 93d Congress and then goes into the 94th Congress, and they eventually passed legislation which went through a conference committee in January 1977. That legislation provided for joint leasing of the 8(g) area. Do you recall that?

Governor WHITE. Yes, sir.

Senator JOHNSTON. Under that legislation, the State and Federal Government had jointly to get together. It provided an effective and total veto to any State that didn't want to lease.

You are talking about all of these grand and glorious funds for the State of California. There would be no funds if you had that legislation, because California would veto. And they said, well, let's don't go on joint leasing. Let us, the Federal Government, lease and we will then divide the revenues fairly and equitably.

And that is the provision which was put in in the next Congress as S. 9 which was reported by this committee. And that provides—that eventually became Public Law 95-372. In effect, what we started off with was joint leasing. That is to say, joint veto by the State and Federal Government. And in lieu of that, we went to allowing the Federal Government to lease with a fair and equitable distribution of the revenues.

Now, one more question, Governor. Failing an agreement between the State and the Federal Government, the money is put

into escrow, not available to either the Federal or State Government until it is decided by a court.

Governor WHITE. That is what we thought.

Senator JOHNSTON. That's right. We thought it was going to stay in that account.

Does the statute provide who must file suit? In other words, does it make it incumbent upon the State to file suit and give you a certain number of days to file suit in?

Governor WHITE. If the Secretary and the Governor cannot agree, as determined by the district court, I presume the Federal court can do it as well.

Senator JOHNSTON. That's right. In other words, it doesn't provide for any burden of proof. It doesn't provide for who files suits. You put the money in the escrow account and the district court will decide what's fair and equitable. And there is no statute of limitation. If the State fails to file suit for 10 years, the money stays there, or if the Federal Government fails to file suit, the money stays there.

Now, there being no burden of proof, no burden of filing a suit, it would seem to me the presumption in the absence of proof ought to be a 50–50 division; wouldn't you think so?

Governor WHITE. One approach would be you slice the pie and I'll choose the piece. That almost keeps everybody honest every time.

Senator JOHNSTON. I think that's an excellent way to put it, Governor. Thank you very much.

The CHAIRMAN [presiding]. Senator Evans.

Senator EVANS. I guess, Governor, the question is how big is the pie before you slice it? And that is the real question. Once you get the size of the pie, then I agree with you that let somebody slice it and the other take the first piece.

Governor WHITE. In this case, the Department of the Interior is in charge of producing the pie. They're the only ones with control of the leasing mechanism. And I think if you will look at the background on that, it may be a subject of concern to this Congress.

Did they maximize the revenues for the Federal Government in the way in which they went about the leasing program? There is serious doubt that they did.

Senator EVANS. The question we must now deal with is, How big is the pie we are going to distribute or cut up, regardless of how wisely or unwisely they gained the amount of money that is now in the account?

And I guess the question—we have had a lot of questioning about whether the money is or isn't there, and whether there is or isn't any budgetary impact.

I think the Secretary was quite accurate in pointing out that if money is distributed from that account to the various States to that degree, the Government then has to go out into the competitive public market to borrow that amount of money.

And I remember as Governor, we frequently had 165 separate accounts in the State treasury. Many of them were in essence the equivalent of escrow accounts. But they were accounting mechanisms. The money was there and available, except that it was in-

vested and very often it was invested in the borrowings of the State.

The State borrowed the money and paid for it. That is as good an investment, I suspect, as any other they might have made, and I suspect that was what happened in terms of the Federal Government.

My concern, Governor, I guess—let me start out by asking—in the past I think it's true there have been Federal tracts from the State of Texas where lessees have drained Federal resources.

Do you think the State of Texas ought to compensate the Federal Government for those drainages?

Governor WHITE. I think you will find the purpose behind this is—or at least my understanding is to compensate the States for the burden we have imposed upon us by the Federal leasing. The infrastructure burdens are real. They are without question. When things go back in the oil and gas industry, you find those impacts continue to be real, and I think that is the underlying basis for the proposals associated with 8(g) and the division of the revenues, and it is my understanding it is not dissimilar to the underlying reason for the 50–50 split on inland States.

And there is no suggestion that there would be any compensation for drainage. I would hope that there would be an active development program on the part of the Department of the Interior. That is the way you compensate for drainage. Let them go develop.

Senator EVANS. Should it be a two-way street or a one-way street?

Governor WHITE. In this case, if they will actively develop, it is a two-way street. They wouldn't have to be worried about the drainage.

Let me say the way in which they have gone about the development creates problems for us on drainage in the sense that one of the offshore tracts that I mentioned earlier on the State side of the line, we leased that tract as a discovery well with a low bonus but a high royalty, 45- to 55-percent royalty.

So what happened is, we encouraged them to go drill, and when they find something we have a higher royalty income. That was a known producing well. The Department of the Interior went in with a known producing well and leased a tract directly offsetting that one for one-sixth royalty.

Now, let's look at what we have done. If this were a corporation that had done that, the shareholders would be outraged because they have given away the farm. They know there's a producing well right there that is drawing a 45- to 55-percent royalty. And for you, as a wise manager and investor of your funds, to go in and use your property and say you are going to lease your side of that line for one-sixth, there would be not only investigations; there would be lawsuits and possibly indictments if it were shown to have been done after full knowledge and information.

Now here's where it comes. You are the owner of—here's where the drainage comes into being. You are the owner of both sides. Which one will you produce, the one with the one-sixth royalty or the one with the 55-percent royalty? Those are the leasing practices of the Department of the Interior, not just the Secretary. It's

been a consistent pattern throughout by some of the Undersecretaries, apparently, that that is the way it should be done.

That is not wise. That is a waste of the Federal resource and that is something that should make Senator Metzenbaum extremely concerned and every other Senator and every shareholder in this country, concerned about that policy.

Senator EVANS. What were the relative bonuses at the time of lease on those two sides?

Governor WHITE. They were much higher.

Senator EVANS. You said low one is on high road. On the other side, was there a high bonus?

Governor WHITE. There was, because these people knew what they had. They had information on what was down the hole on this side of the tract. That was some information that no other company in the world had. It was privileged information to the bidder and they went in and, sure, they bid up a high bonus. They sure did because they wanted to make absolutely certain they got it, because they knew once they got both sides of the line they got to develop the whole area according to their plan.

And, strangely enough, I would suggest that the one-sixth royalty would be a bigger producing well than the 55-percent royalty, based on human nature.

Senator EVANS. I suspect, I have heard there are some in Congress who complain on various occasions about the relationship between royalty and bonus payments, and they suggest the Government is not getting enough, early enough, by putting out a lot of these things at low or no bonuses. So sometimes we may be as responsible as the Department for some of that.

Governor WHITE. I think the Department draws up the plans on that, and I don't think the question should revolve around drainage because I think that has been rejected. In this whole legislation, drainage has been rejected, and it is not the test. And unitization would take care of that as far as the Federal Government is concerned.

Senator EVANS. I listened fairly carefully to Senator Johnston who read that footnote several times, and it appears in your testimony where Judge Parker ordered the Secretary to deposit from lease sales into escrow so that all revenues could be taken into account by the court in arriving at a fair and equitable decision.

It seems to me that for any judge, pending a decision, that is a wise thing to do—corral all of the money before you make the decision. It seems to me that I also heard that he concluded that to the extent that these tracts extend beyond the 8(g) zone, they are beyond the court's jurisdiction in the sense that this court cannot distribute Federal revenue attributable to non-8(g) lands. And in his judgment, I understand that he ruled on nine tracts for bonus enhancement, but Texas claims the 8(g) Federal royalties were dismissed except for claims to drainage.

Is that correct?

Governor WHITE. I'm sorry; I didn't hear the last point.

Senator EVANS. In a judgment entered March 15, 1984, Judge Parker ruled that all of Texas' claims to 8(g) Federal royalties were dismissed except for drainage, except for claims to drainage.

Governor WHITE. I don't think that's right. Pardon me, Senator, but I don't believe that is correct. I don't believe he took that into account. The only issue resolved in that case was the question of enhancement of the bonus.

Senator EVANS. There's nine tracts, bonus enhancement. And the royalty question, the Federal royalties for 8(g) lands, it's my understanding they were dismissed, except for claims to drainage.

Governor WHITE. It was without prejudice. He was trying to dispose of this issue. We were able to raise that issue again. And that is one of the things that Judge Parker said, I think in open court, that the burden they placed on the court to go into all of these fact-findings on divisions of these properties was an extraordinary burden, and he had hoped they could settle this legislatively.

I think he was just dividing that out.

Senator EVANS. I'm not talking about what he may have said in court about hoping we could get to a solution, but what he actually decided. And to that degree, I think there has been some indication here that he decided far more than he actually decided.

Governor WHITE. I don't think he decided anything but the enhancement of those bonuses as far as his judgment is concerned.

Senator EVANS. And that was only on a small portion of the total tracts under litigation.

Governor WHITE. Yes, sir.

Senator EVANS. It dealt with bonus enhancement, and I would really like to find out, Mr. Chairman, whether I am correct in my understanding or not, that in terms of 8(g) lands, in terms of the judgment entered, and as a result the effective ruling that the Texas claims to 8(g) royalties were dismissed except for claims to drainage.

Senator JOHNSTON. No; they said for future leases, the Secretary should deposit in the Federal escrow fund all revenues attributable to such tracts.

Senator EVANS. That's depositing in the fund. It doesn't say how they will ultimately be distributed.

Senator JOHNSTON. That's right. They didn't decide with respect to——

Senator EVANS. What I am trying to elicit, and it ought to be easy to determine, is in the judgment did he or didn't he dismiss claims to Federal royalties?

Senator JOHNSTON. Only the 50-percent Federal share.

Senator EVANS. It's my understanding that he ruled that all Texas claims to 8(g) Federal royalties were dismissed, except claims for drainage.

Senator JOHNSTON. No; what he did was, he divided it 50–50. He said the State may be entitled up to 50 percent of royalties. Put that 50 percent in royalties and let the Federal Government have its 50 percent pending further determination.

Senator EVANS. I think it is important to clear that point up. I have just one more question, Mr. Chairman. I was struck by the various conditions that existed in different kinds of leases, as the Secretary pointed out in the chart that he had there.

At least in one tract offshore from Texas—and I suspect this is true in other States as well—there is one where there are only 9 acres out of almost 6,000 acres which fall within the 8(g) zone, a

$10 million bonus. Does it really make sense? Is that equitable, to have the State of Texas receive 27 percent of a $10 million bonus, when less than 1 percent of the tract——

Governor WHITE. First of all, Senator, the State didn't draw that line that way. The Department has agreed not to do that in the future.

Senator EVANS. I think that was a wise decision.

Governor WHITE. And if all of the oil came from that side of the line, certainly the State would be entitled to it. And yet you don't know if you want to allocate it that way, if you want to prorate it on a make-rich basis, you see a very good example of how they can work the impact through their leasing practices.

They can draw that line as narrowly as they would like. They can also draw that line all of the way down to just off the 8(g) line, and as a result on a proration basis, it would appear that all of the tract was on a Federal site, outside the 8(g) line area if you use the proration theory. But all that is, is an invitation to fraud.

They will use those techniques and they can use them very easily where they know where a well may be along the Texas side of the line.

Senator EVANS. You are suggesting from that that if they draw the line right along the outer edge of the 8(g) line, that the State still ought to have some share of what goes on outside?

Governor WHITE. No; what I am suggesting is, they should follow the pattern they are adopting now. That is, don't let tract lines overlap the 8(g) line. To suggest that you do it arbitrarily or let them draw the lines in any way they fashion is an open invitation to fraud, and I guess the best example I can give you is the oil well.

While we are speaking of it, if there's an oil well on the Texas side of the line and they know it is a producer, they can draw those lines for the next tract of leasing that would be a very narrow strip, extend those lines on the outside of the 8(g) property, and make it just as large as they choose.

And on a proration basis, all of the moneys or a vast majority would be going to the Federal Government, even though the only well they have is setting up against the State's 8(g) line.

Senator EVANS. I understand what you're talking about.

Governor WHITE. I don't think that would be fair.

Senator EVANS. If that's unfair, isn't it equally unfair to reach up and grab a 27-percent share of everything?

Governor WHITE. The point is, the court said until we can determine what you have done, we are going to take all of this money and hold it.

Senator EVANS. I understand they are going to take all of the money and hold it, but that doesn't prejudice whatever decision the judge might come up with. He might give all; he might give none. All he's doing is saying I'm going to keep the whole pot until I make a decision.

Governor WHITE. [Nods affirmatively.]

Senator EVANS. I think to read from that that he has determined that all of this should be included is too large a reading.

Senator JOHNSTON. Well, with respect to bonuses, he did.

Senator EVANS. Bonus enhancements. Bonus enhancements. That's correct. But he put the whole tract with respect to bonus enhancements.

And now you want to extend that to all of these other elements, and that is why I say——

Senator JOHNSTON. You're correct. He did not extend that to royalties. He said hold the 50 percent. That will be sufficient to protect the States.

Senator EVANS. So it seems to me we're reading more into the court decision than is probably legitimate, since we are still really in litigation. And what we ought to do is reach some kind of an equitable legislative solution if we can, if it contains within it the ability to eliminate court suits.

Senator JOHNSTON. That is really what we are trying to do.

Senator EVANS. I understand.

Senator JOHNSTON. They got 50 percent of bonus enhancement which equaled 27 percent overall, but as nonprorated tracts. In other words, using the 27 percent, it equaled 27 percent of the whole thing without prorationing.

Senator EVANS. But you are talking royalties and everything else into it. That goes beyond what the courts have already said.

Senator JOHNSTON. That is correct. The court did not decide that one way or the other on royalties.

Senator EVANS. They said it is a subject of negotiation.

Senator JOHNSTON. But the statute itself provides that royalties be included.

Senator EVANS. But then there is the question of whether that comes or doesn't come under proration.

Senator JOHNSTON. Senator Metzenbaum.

Senator METZENBAUM. First I would like to say to my colleague from Louisiana, you said the statute provides for sharing, but actually the statute says not withstanding any other provision, the Secretary shall deposit in a separate account in the Treasury of the United States, all bonuses, royalties, and other revenues attributable to oil and gas pools underlying both the Outer Continental Shelf and submerged lands, subject to the jurisdiction of any coastal State, until such time as the Secretary and the Governor agree, and if they can't agree, a district court determines the fair and equitable distribution.

That isn't exactly saying it, but it's an indication that they were to be deposited in this escrow account until the court ruled on it, but not all of the amounts you are talking about. They are talking about a limited portion of those accounts.

Senator JOHNSTON. The Department of the Interior now assumes that there is a common pool with respect to all 8(g) tracts.

Senator METZENBAUM. Let me just go on with the Governor.

Governor, can you tell me what tract 67, 69, and 74 are? How would you describe those?

Governor WHITE. Pardon me. I'm sorry, Senator; I am not sure I am familiar with them precisely.

Senator METZENBAUM. They were part of the litigation.

Governor WHITE. In the case in the lease sale.

Senator METZENBAUM. And under the statute, as I understand it, under the proposal of the Senator from Louisiana, the revenues

from those tracts would be distributed on the 27-percent formula; is that correct?

Senator JOHNSTON. Excuse me?

Senator METZENBAUM. Tracts 67, 69, and 74. There would be a 27 percent distribution to the State.

Senator JOHNSTON. 69?

Senator METZENBAUM. 67, 69, and 74.

Governor WHITE. Senator, I think those are the sale numbers and not tract numbers, and they include many tracts.

Senator METZENBAUM. You're right; they are the sale numbers.

Governor WHITE. And they include many tracts.

Senator METZENBAUM. The court, as I understand its orders, said all claims relating to and rising out of Federal lease sale 67, 69, and 74 are severed from this action. That's his order. All revenues, including bonuses, royalties, and other revenues generated by Federal lease sales 67, 69, and 74 are to remain in or be deposited in a separate Treasury account.

Now, I don't understand why, if he has severed them and said that they are not to be distributed but they are to remain in a separate account, I don't understand why you are here saying that you should get 27 percent of them. And that is what I understand your position is, and that is what I understand the legislation provides.

Governor WHITE. That is part of the settlement.

Senator METZENBAUM. And I'm saying to you, what settlement? The court's order. Are we talking about a settlement? The case is not settled at this point, is it, Governor? The case is on appeal. So what settlement are we talking about?

Governor WHITE. The understanding that there would be a division based on a 27 percent figure. That isn't what I asked for. I asked for a 50–50. We countered with 37½ and now in an effort to settle the dispute and resolve the issues, I am agreeing to accept 27 percent based upon all of it, bonuses, royalties and——

Senator METZENBAUM. But the court said you don't have any right at all to these funds.

Governor WHITE. I disagree.

Senator METZENBAUM. No; I won't say he said that. He didn't say that. What he really said is that they are severed from this action and are not a part of this action.

Governor WHITE. He's trying to give us a final judgment appealable on the one issue that he resolved in this case, and that was the issue of bonus enhancement and he is reserving those matters for a later determination.

Senator METZENBAUM. Governor, you have practiced law how long?

Governor WHITE. Twenty years, plus.

Senator METZENBAUM. And, Governor, isn't it the case that in many of those matters in which you have been involved and I was involved as a practicing lawyer, we won some in the lower courts to lose in the upper courts, and vice versa, and that for us to proceed on this basis as if the court had finally disposed of this matter would be premature?

Governor WHITE. No, I don't think so. I think that we have every reason to expect this case to be upheld on appeal. I don't see any reason to suggest it should be otherwise. And I would hope that we

wouldn't have to await the determination of the courts in order to determine a legislative division.

Senator METZENBAUM. What would you think, Governor, if we put into this legislation a clause providing that this is divided however, but that if the appellate court reverses or in any manner changes the decision of the lower court, that that court's decision shall affect directly the statute, and that the statute shall be conformed immediately thereafter in accordance with the court's decision?

Senator JOHNSTON. Upward or downward?

Senator METZENBAUM. Yes, upward or downward. I guess what I'm saying to you is, you might have won in the lower court, and now you want all of the marbles and you want to go beyond that. You want to go into the royalties and taxes as well on the basis of the court's decision.

My point is that you want it, heads I win, tails you lose. And I'm saying to you, well, if you're so much convinced that this court decision does that much for you, then you ought to respect the judicial system and the appellate process as well.

Governor WHITE. Well, let me say the court's decision may appear to have been a complete victory for the State, but I think you will find we were talking about a fair and equitable division of the enhancement bonuses.

I thought we were entitled to 100 percent of the enhancement.

Senator METZENBAUM. I was reading the statement from the fellow who's the Governor of Texas. I think it was Boyd, and he said we won.

Governor WHITE. Well, we did. Let me assure you, as opposed to what the other side said. They were very disappointed they had to provide any enhanced value.

Senator METZENBAUM. In the second year in my term of Governor, the court announced we had won.

Governor WHITE. I think he's right.

Senator METZENBAUM. And what I'm saying now is that if the court should pronounce on appeal that you had lost, or had lost in part, since this legislation is drafted on the basis of that decision, why not permit the court to have the matter and tell its conclusion?

Governor WHITE. Well, maybe a merger of power between the executive, legislative, and judicial might be unconstitutional but——

Senator METZENBAUM. We could draft the legislation in some way to take that into account. I am not worried about the constitutional aspects. There are legislative draftsmen around, like our chairman or the ranking minority member.

The CHAIRMAN. Don't ask the chairman to do it, because I think it's unconstitutional.

Senator METZENBAUM. Well, if we could find a constitutional way to do it, would the chairman look favorably upon such language?

The CHAIRMAN. I would respond to the Senator's question in this light. I intended to make this statement a little later. A fair reading of the judge's decision would also include a reading of his complaint that Congress had handed him an impossible task of determining what was just and equitable, and that the courts aren't designed to do that, and that he couldn't find a way to do that.

And therefore, whatever was going to be done would be arbitrary.

Senator METZENBAUM. Unjust and inequitable.

The CHAIRMAN. He invited the Congress to revisit the question and determine how that issue should be settled. And he said it both on a factual basis and I think also on a political basis. He suggested that Congress should revisit the issue.

Now, that is what we are doing. The question of how we resolve it after we revisit it is the subject of the debate.

Senator METZENBAUM. Governor, what is the basis for the State's claim on royalties in tracts that lie entirely within Federal waters and which don't have common pools with tracts inside the 3-mile coastal zone?

Governor WHITE. Well, you never know. The common pool issue, it's not a very good geologic term. But you will never determine whether the pool is common or not until the field is fully developed. And as I said earlier, that might be 60 years from now, and I don't think either the Federal Government, the States, or the Congress intended that this provision be retrospective after 60 years of experience.

I would allude back to my prior statement about the way in which, leaving all of the discretion with the Department of the Interior, they can manipulate the lines to make certain that you diminish a fair and equitable sharing or any sharing for that matter with a State, by the manner in which they draw those lines.

And I think they corrected that problem by not extending tracts of land over their 8(g) line. I think they have solved that problem. But until they are committed to that position, they can always go back and drive a wedge down into a portion of the property that will effectively deprive the State of any share.

Senator METZENBAUM. Would you agree that if there is no common pool, States should get nothing?

Governor WHITE. No, sir.

Senator METZENBAUM. Do you think the States should get something, come hell or high water?

Governor WHITE. The point, I think, and the underlying issue is this fact that the State is burdened by the production of that oil and gas property, by the infrastructure impacts made along the coast. It is our coastline that gets oil on it. It's our coastline that has to be cleaned. It's our coastline that has to have the harbors, and we have to put up that infrastructure.

It's our coastline that has all of those impacts. It's also the people who are working on those offshore leases, sending children in our State, and we provide the funding for that. I think there is a true justification for——

Senator METZENBAUM. You are also getting the revenues from the 3-mile limit. You are getting them from the next 3-mile limit, the 8(g) area. You are getting the taxes. You are getting the employment that it provides in your community.

And my recollection is—and I don't know whether Texas came into this—but I remember some years ago when my colleague from Louisiana got through a special provision providing for funding for that very purpose, and that is for the impact upon the State of this offshore drilling.

And I would guess, knowing how able he is in protecting his State's interest, that that has probably been in there and been enhanced over a period of years.

Senator JOHNSTON. Unfortunately, that is no longer funded.

Governor WHITE. Yes.

Senator METZENBAUM. Oh, my God, the Federal Government got a break. You got $20 or $200 million?

Senator JOHNSTON. We did, and the coastal energy impact fund—I forget the amount—but the authorized amount was never funded and after about 3 years, it was no longer funded. At about the time we adopted this 8(g) legislation, the 8(g) was meant to cover those very concerns that we had in the Coastal Energy Impact Programs, and it was discussed at the time. And I think you were a member of this committee at that time.

In lieu of having a joint leasing, which would allow a State veto, we went to allowing the Federal Government to lease, but dividing the revenues fairly and equitably. And by the way, it doesn't just say common pools; it talks about fields as well. Fields are much broader.

Governor WHITE. I think the Department of the Interior has also agreed that a common pool is no longer an issue and it should cover all of the 8(g) tracts. So the Department's position is no different on this than the State's.

Senator METZENBAUM. Let me just make an observation to you and to my colleagues. All of them were making great speeches about the fact that they thought there was a pile of money sitting in there and you could walk in and see the gold or the dollar bills sitting in the Treasury.

Any one of us who have been around any period of time at all know that there are Government funds after Government funds. Talk about trust funds, talk about escrow accounts, but there is never that pile of money. It is always used, interest-bearing if you please, by the Federal Government, whether it has to do with Social Security or Medicare or whether it has to do with the FDIC.

What would you expect the Government to do? Sit on it? Put it in a little room, have two people sitting there watching the money? Of course it is invested, and therefore it becomes a part of Government funds, and I thought it was——

The CHAIRMAN. If the Senator would yield on that point, to whatever extent I may have made a comment about that earlier, I don't think the question is whether or not the money is there or whether or not the Federal Government has used the money by investing it in Government securities and therefore having spent it for other purposes.

The question as I see it is whether the Government is in a position now to complain about paying it out to the rightful owners just because they would have to borrow somewhere else.

That would be a little bit like when you file your income tax return and you get a refund coming, to have the Government say I can't give you the refund now because I would have to borrow the money to give you the refund.

Senator METZENBAUM. We borrow so much, it won't matter, a little bit more.

The CHAIRMAN. I wouldn't disagree with the Senator on that point, but I think it's a little disingenuous for the Department to now claim that an equitable distribution of the funds should not be made because the Government would have to go out and borrow the money somewhere else to make up for the borrowing that they have done here.

Senator METZENBAUM. Well, Mr. Chairman, I am going to leave, but I wanted to check with you as to the program for the balance of the day. It is my understanding that Senator Dole will put into effect some rule as to how late we would vote today, by reason of the fact that some of us observe a holiday and leave early for that purpose.

I have tried to be here all morning and I will be here at 3 o'clock, but at a certain hour I would hope—I think there are two members of this committee who observe this holiday, and I would hope that——

The CHAIRMAN. I would hope we can resolve the issues before us on the reconciliation resolution, as I announced in my opening statement, before sundown this evening, which is the appropriate time that we will be able to do that. Of course, I don't know what the committee is going to do and I cannot tell you that I know exactly how quickly or slowly the issue will be resolved.

Senator METZENBAUM. I appreciate the chairman's consideration. I am trying to explain the holiday actions start this sundown, but the holiday is a fast holiday, and members of our faith have dinner prior thereto, so most of us will be pulling out at 4:15 or 4:30.

The CHAIRMAN. Maybe we can have the issue resolved at that time and it won't be a problem.

Senator METZENBAUM. I will be here. Thank you.

The CHAIRMAN. Are there any further questions of members of the committee for either the Governor or witnesses from the Department?

[No response.]

The CHAIRMAN. Apparently there are none at this time. I appreciate the testimony of the Department and of the Governor, and I want to express to you my personal thanks for arranging your schedule so that you could be here on such short notice.

Senator JOHNSTON. My thanks as well.

The CHAIRMAN. I think that perhaps underscores the seriousness and importance of the issue. Thank you very much.

The committee stands adjourned.

[Whereupon, at 11:45 a.m., the hearing was adjourned.]

APPENDIX

Additional Material Submitted for the Record

BILL SHEFFIELD
GOVERNOR

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

September 24, 1985

The Honorable James A. McClure
Chairman
Senate Committee on Energy
and Natural Resources
358 Dirksen Senate Office Bldg.
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for the opportunity to present for the record the views of the State of Alaska regarding Section 8(g) of the Outer Continental Shelf (OCS) Lands Act.

My office has been actively involved in efforts to settle the 8(g) issue for some time. These efforts have included extensive negotiations with the Interior Department, the filing of litigation, and, most recently, active legislative advocacy in coordination with other 8(g) States and our Congressional delegation. In a time of rapidly decreasing State revenues and other considerations, the attainment of a fair and equitable distribution of 8(g) revenues is one of the highest priorities of my Administration. We believe that it is in the interests of both the United States and the States to satisfactorily resolve the 8(g) matter in order to avoid protracted litigation and to release needed revenues to both federal and State coffers.

Enclosed, for the record, are my statements and testimony before the House Interior Subcommittee on Energy and the Environment, and the House Merchant Marine Subcommittee on the Panama Canal/Outer Continental Shelf. Also enclosed are critiques of the Interior Department's position and proposed legislation on section 8(g), and a copy of the complaint filed by the State of Alaska against the United States. These documents fully set out Alaska's position on the section 8(g) controversy.

While there are other issues involved in the section 8(g) dispute that are very important to the States, the controversy has generally centered on two issues: deficits in the escrow account and the percentage of 8(g) revenues that should be distributed to the States. The legislation

before the Energy Committee deals with the latter issue by providing for a distribution of 27 percent of 8(g) revenues to the States. It also provides for division among the States of approximately 27 percent of the existing escrow account. The deficiencies in the account are dealt with by temporarily recouping an additional 10 percent of the federal share of future 8(g) revenues and by distributing it among the States.

I am concerned that acceptance of this legislation, as well as that passed by the House Interior Committee, be recognized as a real compromise by the States. However, without passage of all provisions of the Act, including recoupment provisions, the legislation cannot be considered a fair and equitable division of revenues, or even a fair settlement of the issue.

The issues that this Congress is faced with in distributing the 8(g) escrow account result in large part from actions taken by the Interior Department. We have consistently pointed out that the deficiencies in the escrow account are due to unilateral determinations made by the Interior Department in contravention of a federal district court decision. To compound the problem, these determinations or practices were not consistently applied to the lease sales of the various States. The result is that for some States a much larger percentage of revenues actually received have been placed in escrow than for other States. Simple distribution of the existing escrow account without provision for recoupment would unfairly penalize all States involved. But some, including Alaska, would be more adversely impacted than others.

It is for these reasons that the State of Alaska supports the section 8(g) legislation recently introduced by you and Senator Murkowski. We are advised that this legislation clearly satisfies the directives contained in the budget resolution. Further, while not perfect from the point of view of the Coastal States, I believe that the proposed bill, which is similar to one already reported by the House Interior Committee, strikes a reasonable balance between a number of complex and important considerations.

I do feel, however, that the bill which you have introduced should be amended to increase the initial allocation of funds to Alaska by $10 million. Such an increase is necessary to bring Alaska's share into line with escrow figures compiled by the Interior Department. With adoption of the Texas/Louisiana amendment, this change would mean that each Section 8(g) State would receive the

higher of the Interior Department or CBO per-State allocations. It should also be noted that the increase which we are recommending would not abrogate the Budget Committee's instructions.

In conclusion, the State believes that the best legislative solution to the section 8(g) controversy is one which wisely serves the objectives of the 1978 Amendments. America in 1985 still needs an effective and vigorous program of OCS oil and gas development. We believe that the chronology of 8(g) is a history of federal-state confrontation in which the Department of the Interior has neglected the Congressional mandate for cooperation, as enunciated in two federal court decisions. In our opinion, this Congress should end that unhappy impasse by affirming the rights of the States to share bonus, rent, and royalty income on a fair and equitable basis.

Thank you for your consideration of these views.

Sincerely,

Bill Sheffield

Bill Sheffield
Governor

BILL SHEFFIELD
GOVERNOR

STATE OF ALASKA
OFFICE OF THE GOVERNOR
JUNEAU

July 29, 1985

The Honorable Morris K. Udall
Chairman
Subcommittee on Energy and
the Environment
1327 Longworth House Office Bldg.
Washington, D.C. 20515

Dear Mr. Chairman:

Thank you for the opportunity to present for the record the views of the State of Alaska regarding Section 8(g) of the Outer Continental Shelf (OCS) Lands Act.

Section 8(g) requires the "fair and equitable" division between each state and the United States of revenues attributable to oil and gas leases in the three mile zone adjacent to that state's seaward boundary. The statute further requires that the 8(g) revenues be held in escrow pending state - federal agreement or district court determination on the fair and equitable division of revenues.

Large amounts of revenues have accumulated in escrow since Section 8(g) was enacted in 1978. This has occurred because fundamental differences between the affected states and the Secretary of the Interior have made agreement on the division of 8(g) revenues impossible. Recently, former Secretary Clark proposed that the United States should take 83.33% of all amounts in escrow, and 100% of each of the following: 8(g) revenues which were never placed in escrow, all future 8(g) royalties (other than royalties attributable to drainage of the state's oil and gas), and all other future revenues, such as tax revenues. All seven affected states have rejected that offer. Six states, including Alaska, have proposed a settlement which would divide <u>all</u> 8(g) revenues (not just those in escrow), including bonuses, rentals, royalties, and tax revenues. The states proposed that 37.5% of all revenues be distributed to the affected states, and 62.5% to the United States. In May, Secretary Hodel rejected this offer and suggested that preliminary staff discussions on subsidiary issues be held preparatory to later meetings on the principal issues raised by the governors' counter-offer.

The House budget resolution (H.C.R.152) recommends, directs, and assumes passage of substantive legislation to distribute the revenues being held in the Section 8(g) OCS escrow account, with 73% allocated to the federal government and 27% allocated for distribution to the affected states, in order to provide $4 billion in additional federal revenues for FY 86. Although the Senate budget resolution contains no comparable provision, a consensus seems to have emerged among House and Senate Budget Committee conferees and Administration officials to settle the Section 8(g) issues along the lines suggested in the House Budget Resolution.

From Alaska's perspective, there are two major problems with the House proposal. First, the Interior Department has failed to put the proper amount of money into escrow. Second, the fair and equitable share for Alaska and other 8(g) states is at least 37.5% of the total amount that should properly have been placed in escrow.

(1) The Interior Department has failed to put the proper amount of money into escrow. The amount held in escrow is significantly below what should be there. Because of this fact, the House Budget Resolution's exclusive focus upon the percentage allocation of the revenues is inappropriate.

When the 8(g) escrow account was first established, the Interior Department properly placed into escrow bonuses from all tracts which included any acreage within the 8(g) zone. Since that time, however, Interior has adopted two restrictive policies which have artificially reduced the amount in escrow, to the detriment of the states.

Under the first policy, Interior prorates bonus revenues for tracts straddling the 8(g) line on a surface acreage basis, even though the potential production may all originate from the portion of the tract within the 8(g) zone. Under the second policy, Interior has put into escrow only bonuses from lease tracts which it has unilaterally determined have a "capability" of containing oil and gas. In accordance with this approach, Interior does not escrow any bonuses from many tracts within the 8(g) zone. That is, for many tracts within the 8(g) zone, Interior has put no bonus money into escrow, based upon its assessment that those tracts have no hydrocarbon potential. Interior reaches this conclusion in spite of the fact that oil companies have bid substantial sums premised on their assessment that these same tracts have oil and gas potential.

In August, 1983, U.S. District Court Judge Robert Parker ruled that the escrow provision of section 8(g) requires Interior to place all 8(g) revenues into the escrow account. Interior's failure to escrow substantial 8(g) revenues under its proration theory and unilateral geological assessment

violates Judge Parker's reasoning and the plain meaning of the statute.

As of March 31, 1985, the shortfall in the escrow account for all states was more than 1.3 billion dollars, exclusive of interest. The total 8(g) revenues in escrow for Alaska should be 615 million dollars, whereas only 163 million dollars are currently in escrow for the state. The fact that Interior has only one-fourth the amount in escrow which should be there for Alaska, demonstrates the problems of simple percentage allocation. It is essential that serious attention be afforded to the issue of what revenues must be divided.

(2) The fair and equitable share for Alaska should be at least 37.5%. Alaska believes that any legislative settlement of the Section 8(g) issue should provide the states with a percentage of the funds which should have been placed into the escrow, not just the amount that is currently there. Moreover, we believe that, absent special circumstances, the fair and equitable division of revenues would be an even division between the United States and Alaska. Accordingly, Alaska's participation in the 37.5% offer is a significant compromise by the State.

Alaska's own leasing program, which has resulted in the current production of over 1.7 million barrels per day from State lands, has done much to enhance the value of federal OCS acreage. Additionally, the impacts of OCS development, both in human and environmental terms, fall heavily on Alaska's coastal residents. For these and other reasons, the 27% figure proposed by the House Budget Committee is unacceptably low.

If Congress is going to resolve the 8(g) dispute through legislation, the problems discussed above must be addressed. There are also other considerations that should be dealt with in substantive legislation. Among them is the need for adequate sharing of information with the states by the Interior Department. Alaska will also want to clarify its entitlement to 8(g) funds in the event that the United States is successful in the Beaufort Sea boundary litigation. We have discussed these issues with Congressional staff in the past. We would hope to continue to work with you and your staff in the future to reach a successful resolution of these issues.

Thank you for your consideration of our views.

Sincerely,

Bill Sheffield

Bill Sheffield
Governor

cc: The Honorable Ted Stevens
The Honorable Frank Murkowski
The Honorable Don Young

For the record, I'm the Governor of Alaska, Bill Sheffield. Before I begin my testimony, I'd like to welcome the members of this committee to Alaska, and I wish you an enjoyable stay in our great state.

As the State's chief executive, I would like to address a couple of major OCS policy issues today. I'll concentrate on these two areas:

* First, the State's request to delay the proposed North Aleutian OCS Sale until at least 1994;

* And Second, our efforts to secure Alaska's fair share of federal OCS revenues.

Alaskans have strong feelings on these issues. Perhaps the best illustration of that came in early June, in the Bristol Bay villages of King Salmon and Naknek. I brought Secretary

of the Interior Don Hodel to that region so he could see and hear the people who depend - every day - on the resources of Bristol Bay.

The plain talk and deep sincerity of those people had a profound effect on Secretary Hodel. When he left those villages, he told me he left with a troubled mind.

The people told him why OCS Sale 92 - The North Aleutian Basin Sale - should be delayed at least until 1994. The State agrees with those arguments, and today I would like to submit to you, for the record, the State's position paper on the North Aleutian Sale as proposed by the Department of the Interior. But let me take a few moments to summarize the highlights of the State's position, and clarify why I'm pushing so hard for the delay of that sale.

Bristol Bay is one of the richest fishing grounds not just in Alaska, not just in North America, but in the world. It also contains one of the greatest concentrations of birds, fish, and marine mammals on the North American Continent.

Hundreds of millions of salmon migrate through the sale area each year. In addition, studies indicate that, in peak years, the sale area and adjacent waters may be the major feeding and rearing area for as many as a billion outmigrating juvenile salmon from Western Alaska, Bristol Bay, and the Alaska Peninsula streams.

That salmon fishery is worth more than a quarter of a billion dollars a year, and provides employment for 10,000 people. Here in Alaska, the fishing industry is the largest private employer, and the Bristol Bay fisheries account for roughly a quarter of the industry's jobs.

The Bristol Bay area is important not only for its migrating salmon, but also for the spawning herring, king crab, and groundfish populations the sale area supports.

In 1982 more than 44 million pounds of herring sac-roe were harvested in Bristol Bay, with a value of more than $6.3 million.

Nearly 70 percent of all red king crab harvested in the eastern Bering Sea comes from the proposed sale area. And perhaps even more important, about half of the domestic and joint venture catch of such bottomfish species as yellowfin sole, pollock, and halibut comes from this area.

I'll tell you why this is so important. One of the goals of my Administration is to eventually eliminate foreign fishing within American waters. We're still in the early stages of

developing our bottomfish industry, but the "American-ization" of that fishery is a top priority.

In fact, the commercial fishing seasons provide the single largest infusion of cash to the people of the region. For many families, the money they make during the commercial season accounts for almost their entire annual cash income.

Let me also emphasize that in Bristol Bay, many people still live off the land. Their subsistence harvest of fish, marine mammals, birds, eggs, caribou, and moose can't be replaced by a trip to a supermarket, especially when the supermarket is hundreds of miles away.

Any offshore oil and gas exploration and development poses risks to fish and wildlife, especially in the marine and estuarine areas close to shore. Those impacts include oil contamination from spills, pollution from drilling muds,

habitat alteration from construction activities, and noise and disturbance. We know that even a small amount of oil can have a significant impact.

Industry has come a long way in improving oil spill containment and cleanup technology. But there's still a considerable difference of opinion over whether existing technology or sufficient equipment is available to contain and clean up a major offshore spill in the Bering Sea.

The stakes, and the risks, are high in Bristol Bay. Given the fact that our present data indicates relatively low potential for oil and gas, we believe Bristol Bay should be the last area of Alaska's outer continental shelf opened to leasing.

And, even before we agree to that, we need some major questions answered. As part of our response to the Sale 92

draft environmental impact statement, the State identified 38 important information needs. Fish and Game Commissioner Don Collinsworth will address that information gap in greater detail at your hearing Wednesday in Kodiak.

He'll tell you that yes, there is some information available on some of the topics that concern us. But the available information on many fish and wildlife species is simply not sufficient to reasonably assess the impacts of potential oil and gas development.

Our insistence on a delay for Sale 92 is a stand not taken casually.

Our request to delay Sale 92 is consistent with the State's own oil and gas leasing plan -- and is consistent with the Bristol Bay Cooperative Management Plan, which underwent hundreds of hours of public scrutiny.

My Administration is a solid and active supporter of oil and gas development. During my tenure in office, we've either held or cooperated in 15 competitive lease sales -- ten by the State, and five by the federal government.

We've approved a dozen exploration plans in the Navarin Basin, Norton Sound and St. George federal lease sale areas. And, we're working well with the federal government on several upcoming sales.

We understand that the basins off Alaska's shore can play a major role in meeting our nation's need for domestic oil and gas supplies. And, we're prepared to help meet that national need.

We believe the State and the federal government should be working in partnership in developing our OCS resources.

Which brings me to the matter of recognizing that partnership by sharing the benefits of OCS development.

Section 8(g) of the OCS lands act says the State should get "fair and equitable" share of the money made on federal OCS leases in those three miles just adjacent to the State's three mile limit.

Furthermore, the section says that 8(g) revenues should be set aside, in escrow, until the federal and State governments, or the courts, agree on what constitutes a "fair and equitable" split.

There's a considerable amount of money in that escrow account today, because of fundamental differences between the affected states and the Secretary of the Interior, and how it's divided up is of great concern to Alaska and the six other affected coastal states.

Recently, former Secretary Clark proposed that the United States take 83 1/3 percent of the amount in escrow, and 100 percent of other revenues which we believe should be a part of the escrow account. The individual states would get the remaining.

All seven affected coastal states rejected that offer as far too low. Six of us proposed what we consider to be a fair settlement, that we receive at least 37 1/2 percent of all 8(g) revenues, not just those in escrow...and including bonuses, rentals, royalties, and tax revenues. In May, Secretary Hodel rejected this offer.

Since then, Congress has identified that money in the escrow account as a source of additional funds to further reduce the federal deficit this year. The budget resolution passed by Congress last week assumes passage of substantive legislation to distribute those monies, with the affected states

getting 27 percent and the remainder going to the federal government. That split would provide $4 billion in additional federal revenue for this next fiscal year.

While we commend the spirit of compromise exhibited in that resolution, Alaska still has two major problems with it. First, the Interior Department has failed to put the proper amount of money into escrow. Second, the fair and equitable share for Alaska and other 8(g) states is at least 37 1/2 percent of the total amount that should properly have been placed in escrow.

As to our first point, the amount held in escrow is significantly below what should be there. Because of this fact, the budget resolution's exclusive focus upon a percentage allocation of the amount currently in escrow is inappropriate.

When the 8(g) escrow account was first established, the Interior Department properly placed into escrow bonuses from all tracts which included any acreage within the 8(g) zone. Since that time, however, the Interior Department has adopted restrictive policies which have artificially reduced the amount in escrow, to the detriment of the states.

In contrast to Interior Department practices, a Texas U.S. District Court has ruled that the Interior Department had to place all 8(g) revenues into the escrow account. Interior's failure to do so violates the reasoning behind that court ruling.

As of the end of this March, the shortfall in the escrow account for all states was more than $1.3 billion, not counting interest. We believe the total revenues that should be held in escrow for Alaska should be $615 million, whereas only $163 million are currently in that account.

The fact that the Interior Department has only one fourth the amount in escrow which should be there for Alaska demonstrates the problems of a simple percentage allocation as provided for in the budget resolution. It's essential that serious attention be given the issue of what revenues must be divided, and that the states receive a percentage of the funds which should have been placed into the escrow account, not just the amount that is currently there.

Our second point is that the fair and equitable share for Alaska should be at least 37 1/2 percent. Actually, we believe that our fair share is an even division between the United States and Alaska, so our decision to push for 37 1/2 percent was significant compromise by the State.

Alaska's own leasing program, which has put into production more that 1.7 million barrels of oil per day from State lands, has done much to increase the value of federal OCS

lands. Additionally, the impacts of OCS development, both in human and environmental terms, fall heavily on Alaska's coastal residents. For these and other reasons, the 27 percent figure is unacceptably low.

If there is to be a legislative resolution of the 8(g) dispute, the problems I've just discussed must be addressed. We also must deal with several other issues, including the need for adequate sharing of information with the states by the Interior Department.

Alaska will also want to make clear its entitlement to 8(g) funds if the United States is successful in the Beaufort Sea Boundary lawsuit.

We've discussed a lot of these issues with congressional staff and members in the past. I give you my pledge that we

will continue to work with you and your staff in the future to reach a successful resolution of these issues.

I appreciate the opportunity to testify today, and I'd be happy to answer any questions you may have, as will two of my staff members, Jim Eason, Deputy Director of the Division of Oil and Gas, and Assistant Attorney General Mark Worcester of the Department of Law.

Following your questions, Bob Grogan of the Division of Governmental Coordination will provide further State testimony on additional topics being considered by your committee.

STATE ANALYSIS OF INTERIOR DEPARTMENT'S DRAFT BILL ON 8(g)

The purpose of this analysis is to present reaction of the states of Alaska and Texas to the DOI draft bill on § 8(g). Before addressing specific paragraphs of the draft, it is important to focus on two preeminently important issues which run throughout the proposed bill--the issues of surface acreage proration which is principally responsible for the deficit in the escrow account, and royalty division.

Prorationing and Royalties

Throughout the DOI bill, the agency proposed that revenues be computed on a per acre basis and that the total then be prorated at the outset - prior to division - based on the number of acres within the 8(g) zone. This concept of proration has been the source of enormous confusion and dispute between DOI and the states. The problem - from DOI's perspective - arises because a tract may lie partially within and partially beyond the 8(g) zone. The states say that if a problem exists, DOI created it because DOI controls the size and shape of its offshore tracts. In fact, internal DOI memoranda show that the question of whether or not to draw tracts to conform to the 8(g) zone was debated at length at the Assistant Secretary level shortly after 8(g) was enacted.

The agency consciously chose to permit the overlap to occur. It is neither necessary nor appropriate to now go through the tedious and controversial proration process. The best course, and the simplest, is to divide the current escrow account without considering prorationing. When both Judge Parker and Judge Mentz considered this approach in the Texas and Louisiana 8(g) litigation, they rejected DOI's proposal and concluded that revenues should not be prorated just because DOI chose to let the tracts overlap the 8(g) zone. The states urge

that the lead of the two district courts be followed here. As a practical matter, this would no doubt lead DOI to draw the tracts so as to avoid that problem in the future.

When DOI proposes to give the States a royalty share to compensate them for drainage, DOI offers nothing of significance. First, the states did not need 8(g) to protect them from drainage. Traditional unitization agreements had been used by DOI and Louisiana for many years before 8(g) was adopted. Second, in any event, compensating states for drainage of their own oil and gas is simply paying them for what is theirs to begin with.

In an early opinion, issued shortly after the 8(g) program began, the Department's solicitor advised the agency leadership that 8(g) clearly made all lease revenues available for division and that specifically included royalties. A real share of federal 8(g) royalty income is absolutely indispensable to the coastal states. Royalty income is the only revenue being divided here which is continuing in nature. Consequently, it is the only income which is available, over time, to assist the coastal states in dealing with ongoing production and development activity on the federal OCS. That activity hasn't even begun on a tract when bonuses are paid. The apparent demise of the other financial programs designed to help states deal with the OCS activity only serves to enhance the importance of treating the coastal states "fairly and equitably" on the royalty issue.

Comment Upon Specific Provisions

The comments which follow are referenced to specific sections and paragraphs of the DOI draft.

1. § 1(a). DOI has already conceded that the numbers appearing in this paragraph are wrong. None of the states is going to be willing to accept any specific dollar figure without the right to audit the 8(g) accounting. Moreover, these numbers reflect DOI's practice of prorating bonuses and rents. This practice, unilaterally adopted by DOI, results in a significant shortfall in the money that should be in the escrow account and which should be subject to "a fair and equitable" division. Royalties are excluded and must be included. Further, DOI has already effectively abandoned the requirement to funnel 50% of the monies to local governments and now simply seeks recognition in the committee reports that states should be mindful of coastal communities.

2. § 1(b)(c)(d). These sections would require the states to relinquish any existing 8(g) litigation claims within sixty days after enactment of the bill in order to receive 8(g) funds from the distribution of the current escrow account. This type of provision is punitive and unfair. The 1978 Amendments required Interior to deposit all bonuses, royalties, and other revenues from tracts that included 8(g) leases. Interior has not deposited certain bonus and rental revenues into the escrow account. The states' right to litigate should be preserved unless the legislation provides for a comprehensive and fair settlement involving distribution of all revenues that should have been deposited into the escrow account. Moreover, two of the three states now in litigation cannot legally unilaterally dismiss that pending litigation.

3. § 1(e). This section permits distribution of 8(g) bonuses and rents to

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Alaska upon resolution of section 7 boundary disputes concerning sales 71 and 87. It is unacceptable for three reasons. There should be no prorationing of revenues before distribution. The state should receive 37½ percent of the revenues rather than the 27 percent provided for. Most important, the section does not provide for distribution of 8(g) funds after resolution of the Beaufort Sea section 7 dispute. Alaska is entitled to 8(g) revenues in the event the federal government is successful in this boundary litigation.

4. § (g)(1)(A), (B). Prorationing is inappropriate. Additionally, many of the affected states believe that an equitable division is 50% of all revenues, just as onshore states receive under the Mineral Leasing Act. The counteroffer by the Governors at 37 ½% was a concession reached only after intense and heated debate. A figure below that has been approved by any state except Louisiana.

5. (g)(1)(C), (D), (E), (F), (G). The concepts contained in these paragraphs are acceptable except as to prorationing and the percentage figures used.

6. (g)(2)(A), (B). The states strongly believe that a "fair and equitable" resolution requires a share of federal royalties beyond compensation for drainage.

7. (g)(2)(C). Giving DOI the unrestrained authority to define when and how

drainage will be recognized and compensated, which this paragraph does, is completely unreasonable. The OCSLA currently provides DOI adequate authority for federal lands. When issues arise between adjacent landowners, as here, they are better addressed through traditional methods like unitization agreements. Arbitration is frequently used in those agreements, but the venue and review standards set out in this paragraph deny both the states and DOI any effective judicial review.

8. (g)(2)(D). This paragraph must be changed to reflect that the division of royalties is to be on a percentage basis in addition to compensation for drainage.

9. §8(g)(2)(E)(F). Credit of royalties not disposed of under (g)(2)(D) to the miscellaneous receipts fund is acceptable provided necessary changes described above are made in (D). Treatment of revenues from sales of royalties taken in kind as royalties is acceptable.

10. § 8(g)(3). This section is unacceptable for several reasons. It appears to allow sharing of geologic information only from areas within the 8(g) zone. Interior has acknowledged that information derived from outside of the zone, but related to it, is necessary to an understanding of the 8(g) zone. The states must have the opportunity to share in that information as well. The suggestion that any revenues should be withheld in connection with sharing information is also unacceptable. Further, the secretary should be

specifically authorized to sign a reciprocal confidentiality agreement with the states containing all of the safeguards required from the states under § 26 of the 1978 Amendments (43 USC § 1356).

11. (g)(4). DOI asks the Congress to effectively deny the states any voice in management of OCS leasing programs off their coasts. This paragraph flies in the face of the spirit of the 1978 Amendments which sought to create a cooperative and consultative process. DOI has all of the authority necessary to manage the OCS. This paragraph is a retreat from the consultation and cooperation called for under the 1978 Amendments.

12. (g)(5). Current law contains an anti-injunction provision. Therefore, this provision is unnecessary.

13. (g)(6). DOI has effectively abandoned this paragraph.

CONCLUSION

Alaska and Texas believe that the DOI draft legislation represents a significant departure from existing precedent and statutory law. Further, many of the proposed solutions contained therein would abrogate traditional federal-state relationships or fly in the face of the prior Congressional directive that all 8(g) revenues be shared on a "fair and equitable" basis. For these reasons we respectfully suggest that the DOI bill cannot be accepted either as a mark-up vehicle or as a balanced resolution of the current dispute.

BILL SHEFFIELD
GOVERNOR

State of Alaska
OFFICE OF THE GOVERNOR
WASHINGTON, D.C.

August 28, 1985

TRANSMITTAL MEMORANDUM

TO: THE HONORABLE TED STEVENS, U.S. Senate
THE HONORABLE FRANK MURKOWSKI, U.S. Senate
THE HONORABLE DON YOUNG, U.S. Representative

FROM: JOHN W. KATZ, Director of State/Federal Relations
and Special Counsel to the Governor
MARTHA FOX, Special Assistant Attorney General

SUBJECT: SECTION 8(g) ISSUE PAPER

Attached is the response of the State of Alaska to particular issues raised by the Interior Department, concerning proposed 8(g) legislation.

Please contact us if you have any questions.

Attachment

cc: Rick Agnew
Greg Chapados
Tom Roberts

August 28, 1985

RESPONSE TO POINTS RAISED BY INTERIOR DEPARTMENT ON PROPOSED 8(g) LEGISLATION

The Interior Department has distributed to the State of Alaska an outline entitled Talking Points, 8(g) Legislative Proposal, Department of Interior recommendations regarding 8(g) legislation. It is our understanding that this outline has also been circulated to several committee staffers in Congress. The following is a statement of the points raised by Interior and the State of Alaska's response to each. We are also attaching a copy of our proposed 8(g) legislation.

1. Legislation should be specific in resolving all claims to existing Section 8(g) funds. Alaska is amenable to a legislative settlement of all existing claims with one important proviso. The legislation should recognize current deficiencies in the escrow account and should provide for payment to the states of amounts based on the 8(g) funds that should have been placed in escrow rather than the amounts actually placed into escrow by Interior. Attached to this document, along with our proposed legislation, is a chart showing the amounts received for 8(g) leases, the amounts placed in escrow by Interior, and the amounts that we believe should have been placed in escrow for affected states. In connection with this issue, it should be noted that there are serious legal issues concerning the ability of the Congress to mandate a retroactive resolution of the escrow account issue that is accomplished without the express consent of each affected state, or is in conflict with a standing court order. [See U.S. District Court decision in Texas v. Hodel, 580 F. Supp. 1197 (1984), which is currently on appeal to the Fifth Circuit Court of Appeals.]

2. 73/27 percent Federal/State split of current bonuses, rents and accrued interest. Alaska has consistently taken the position that, while we believe that a fair and equitable settlement would be a 50/50 split between the United States and the State, we are willing to compromise and accept 37½ percent of all bonuses, rents and royalties from 8(g) leases in Alaska. We believe that this is a reasonable position, particularly when the social and environmental costs of federal OCS development will fall on the State and, primarily, its coastal residents. Furthermore, Alaska's own leasing program has done much to enhance the value of federal OCS acreage.

   a. Specific dollar settlements to each State should be itemized in the legislation to preclude further disagreement and litigation. While agreement on specific

dollar settlements for the amount currently in escrow is a reasonable goal, we would object to any attempt to preclude our litigating the issue of the amount that should properly have been deposited in escrow, if that issue is not adequately dealt with in legislation. In practical terms, we question whether it would be possible to complete calculations on specific dollar amounts within the time constraints involved. We believe that if the theory for calculating the dollar amounts is adequately set out, it should be possible to agree on distribution of the amounts currently in escrow.

b. Bonuses would be allotted proportional to the surface acreage of blocks independent of whether they contain a common reservoir. Interior's position on this point combines two concepts, which we will describe as the "proration" and "common pool or field" concepts. Interior's position represents the continued insistence upon improper "proration" and an abandonment of its improper "common pool or field" theory. Alaska appreciates and supports Interior's abandonment of the latter theory. However, the State continues to oppose the improper "proration" theory. The history of Interior's handling of the escrow accounts will help put these issues into perspective.

Proration: In the period immediately subsequent to the enactment of Section 8(g), Interior put into escrow all bonuses, rents and royalties attributable to all 8(g) tracts. Later, however, Interior unilaterally reduced its deposits of bonus money into escrow based upon its "proration" theory. That is, for each 8(g) tract, Interior allotted revenues according to the proration of the surface acreage within the 8(g) zone. For Alaska, this has had a dramatic impact on the amount in escrow. That amount should be at least $633,000,000. However, only about $163,000,000 is now in escrow for the State. Of the difference, approximately $425,000,000 is attributable to the unilateral exclusions of bonus money by Interior based upon its proration theory. The proration theory is not supported by any provision within Section 8(g), and has been expressly repudiated by the United States District Court in Texas.

Common pools or fields: In the summer of 1984, Interior instituted the policy of excluding from the escrow accounts all revenues attributable to those 8(g) tracts where Interior perceived no hydrocarbon potential. However, Interior's assessment that these 8(g) tracts had no hydrocarbon value is disproved by the very fact of the receipt of substantial bonus bids from oil companies for the right to explore these tracts. Accordingly, it is a welcome development that Interior has conceded that the escrow accounting should be adjusted to include revenues from

all tracts, irrespective of Interior's estimates of oil and gas potential.

c. Revenue from blocks between two States where there is overlapping 8(g) acreage would be allocated proportional to the overlapping acreage. Alaska takes no position on this issue.

3. Legislation should be prospective as well as retrospective. Payments to States would be for 27 percent of bonuses and rentals. Alaska has no objection to a prospective settlement of the distribution of 8(g) funds, provided that the legislation contains appropriate guidelines.

a. Funds from 8(g) tracts would be prorated between acreage within and beyond 3 miles seaward of the State boundary on a proportional basis and payments to the States would be made only for acreage within 3 miles of the State boundary. As discussed previously, Alaska has consistently opposed the prorationing of 8(g) funds on the basis of surface acreage within the 8(g) zone. There is nothing in Section 8(g) which supports this approach.

b. If an 8(g) tract is within 3 miles seaward of two States, each State should receive 13.5 percent of the amount deposited for each acre within the 8(g) zone of both States. Alaska takes no position on this issue.

c. When Federal/State seaward boundaries are in dispute, the appropriate percentage of future bonuses and rents from disputed blocks plus interest would ultimately be paid to the States based on resolution of the boundary issues. Alaska agrees with this approach, provided that the money is held in escrow pending resolution of any boundary issues. Alaska has an additional concern, addressed in our proposed legislation, that relates specifically to existing Beaufort Sea boundary litigation and the State's entitlement to 8(g) funds. Under our approach, a percentage of the funds currently held in the Section 7 title account would be transferred to the Section 8(g) account if Alaska loses the current boundary dispute.

d. When the lateral offshore boundary between two States is in dispute, 27 percent of the future bonuses and rents from disputed blocks plus interest would ultimately be paid to the States based on resolution of the boundary issues. Alaska takes no position on this issue.

4. Royalties should be paid to compensate for drainage only. Alaska has consistently opposed this approach to the division of 8(g) royalties. The states already own the oil and gas originally in place beneath state lands. The states also had available various mechanisms for assuring the receipt of revenues for production of that oil and gas before Section 8(g) was enacted. Section 8(g) clearly entitles the states to share in a fair and equitable distribution of revenues from 8(g) leases attributable to the federal interests that are sold, rather than just receiving compensation for state interests that might be exploited.

Any other interpretation of Section 8(g) would ignore the substantial body of law and practice concerning drainage that was already applicable when this section was enacted.

a. The Secretary should be authorized to prescribe methods and regulations to determine common reservoirs and allocations of production. Alaska does not object to the Secretary's promulgation of methods and regulations to guide him in negotiating with the states. However, the determination of the parameters of reservoirs and the allocation of production should not be unilaterally made by the Secretary. There is an established body of case law and procedure to follow when parties are seeking agreement on proper allocation.

b. Legislation should protect against injunctions on leasing, exploration or production on the basis of disputes arising from the legislation. There is no evidence on the basis of past litigation that this provision is necessary. To date, courts have generally viewed the escrow account as adequate protection in the face of an 8(g) dispute over distribution of revenues. If the suggested provision is enacted, it should not preclude injunctive relief when a dispute is also based on other statutory considerations, such as environmental concerns.

c. Fifty percent pass through of funds to local governments which are adjacent to leased areas. Alaska opposes this provision. It is up to a state, not the federal government, to determine the proper distribution of 8(g) revenues within that state. In many cases, a state may have already put into place mechanisms to deal with 8(g) development impacts. This provision would be both unnecessary and obstructive of that process, and would seriously infringe upon state sovereignty.

d. All funds collected by the Federal Government to be shared with States should be kept in an interest bearing account. The Department of Treasury is to determine the specifics regarding accounting. We agree that the money should be placed in an interest bearing account. To the extent that Treasury determines the accounting specifics, the Department should be required to do so in keeping with accepted accounting practice. The states must retain the usual capacity to periodically audit 8(g) accounting records.

5. Information Sharing. One issue that was not raised in the Interior outline, but is of particular importance to Alaska, is the ability to receive adequate information from Interior derived from areas immediately adjacent to the 8(g) zone. To date, Interior has supplied data derived from the 8(g) zone itself. However, the Department has been unwilling to supply information derived from areas outside the 8(g) zone, even though Interior's representatives have conceded that this

information is necessary to a geological analysis of the 8(g) zone. The states have an excellent record of maintaining the confidentiality of this type of information. Because Interior has applied an unduly restrictive interpretation of 8(g) information-sharing requirements, Alaska has had to make costly expenditures to obtain information that, under a reasonable interpretation of the statute, should have been supplied to the State. We will be seeking clarification of the 8(g) language to make it clear that states are entitled to this type of information.

COMPARISON OF ESTIMATED TOTAL 8(g) REVENUES WITH ESCROWED 8(g) REVENUES
AS OF MARCH 31, 1985

	BONUSES	RENTS	ROYALTIES	INTEREST	TOTAL
Total 8(g) Revenues Actually Collected	5,074,958,736	12,168,542	182,298,415	2,430,194,832	7,699,620,525
Escrowed 8(g) Revenues in Treasury Account	3,712,757,841	12,168,542	182,298,415	1,893,275,094	5,800,499,892
Difference Between Total and Escrowed 8(g) Rev.	1,362,200,895	0.00	0.00	536,919,738	1,899,120,633

COMPARISON OF ALASKA ESTIMATED TOTAL 8(g) REVENUES AND ESCROW 8(g) REVENUES
AS OF MARCH 31, 1985

	BONUSES	RENTS	ROYALTIES	INTEREST	TOTAL
Total 8(g) Revenues Actually Collected	532,628,020	2,024,228	0.00	98,183,870	632,836,118
Escrowed 8(g) Revenues in Treasury Account	133,854,480	2,024,228	0.00	27,475,181	163,353,889
Difference Between Total and Escrowed 8(g) Rev.	398,773,540	0.00	0.00	70,708,689	469,482,229

NOTE: All figures used are subject to verification. Figures used to estimate total 8(g) revenues and escrowed revenues for all states were developed by consultants employed by the State. Although the 3/31/85 escrow account figures from MMS apparently did not reflect a proration of rents, it appears that MMS may now be proposing to "adjust" the escrowed rents figure to reflect proration. The State and MMS are currently seeking to reach agreement on applicable figures.

PROPOSED AMENDMENT TO SECTION 8(g)

Sec. 1. Section 8(g) of the Outer Continental Shelf Lands Act (43 U.S.C. 1337(g)) is amended to read as follows:

"(g) Leasing of lands within three miles of seaward boundaries of coastal States

"(1) At the time of soliciting nominations for the leasing of lands within three miles of the seaward boundary of any coastal State, and subsequently as new information is obtained or developed, the Secretary shall, in addition to the information required by section 1352 of this Title, provide the Governor of such State -

(A) an identification and schedule of the areas and regions proposed to be offered for leasing;

(B) all information from all sources concerning the geographical, geological, and ecological characteristics of such regions;

(C) an estimate of the oil and gas reserves in the areas proposed for leasing; and

(D) an identification of any potentially hydrocarbon-bearing area or areas [~~field, geological structure, or trap~~] located wholly or partially within three miles of the seaward boundary of such coastal State, including, where such potentially hydrocarbon-bearing area [~~field, geological structure or trap~~] lies partially within and partially beyond the area within three miles of the seaward boundary of such coastal State, all information relating to the entire potentially hydrocarbon-bearing area [~~field, geological structure or trap~~].

The confidentiality provisions of section 1352 of this Title shall apply to all information provided under this paragraph.

"(2) Notwithstanding any other provision of this subchapter, the Secretary shall deposit into a separate account in the Treasury of the United States all bonuses, rents, and royalties generated by any lease of any federal tract which lies wholly or partially within three miles of the seaward boundary of any coastal State. Within 30 days of the end of each calendar quarter, the Secretary shall transmit to such coastal State 37 1/2 percent of those revenues, together with all accrued interest. The balance of the bonus and rent revenue shall be transmitted simultaneously to the miscellaneous receipts account of the United States Treasury, but the balance of the royalty revenues shall be held until divided and distributed in accordance with paragraphs (3) and (4) of this subsection.

"(3) Each coastal State shall have an additional claim for drainage of its hydrocarbon resources against the remaining federal revenues from lease tracts wholly or partially within three miles of the seaward boundary of such State. Whenever the Secretary or the Governor of a coastal State determines that a common potentially hydrocarbon-bearing area may underlie the federal and state boundary, the Secretary or the Governor shall notify the other party in writing of his determination and the Secretary shall provide to the Governor notice of the current and projected status of the tract or tracts containing the potentially common hydrocarbon-bearing area.

If the Secretary has leased or intends to lease such tract or tracts, the Secretary and the Governor of the coastal State shall enter into an agreement to divide the revenues from production of any potentially common hydrocarbon-bearing area, by unitization or other royalty sharing agreement, so as to compensate the coastal State for the value of its hydrocarbons originally in place under State lands. Where the Secretary and the Governor are unable to agree either as to the existence of a common potentially hydrocarbon-bearing area or the method of compensating the State, the matter shall be decided by arbitration. For that purpose, the Secretary and the Governor shall each select a represenative; in turn, the two representatives shall agree upon an independent and knowledgeable third party who shall be empowered to resolve any disputes as to the terms of the agreement. All royalties generated by a lease wholly or partially within three miles of the seaward boundary of a coastal State containing a potentially common hydrocarbon-bearing area, exclusive of the potentially common hydrocarbon-bearing area, exclusive of the 37 1/2 percent distributed to the coastal State under paragraph (2) above, shall remain in escrow in the separate Treasury account until such time as the agreement contemplated by this paragraph shall be signed by both the Secretary and the Governor. Thereafter, distribution of the remaining 62 1/2 percent of the royalties from said lease shall be as provided by the terms of the agreement.

"(4) When the Secretary offers for lease a tract which lies wholly or partially within three miles of the seaward boundary of two or more states, the revenues from such tract shall be deposited in a specially designated separate account segregated from other revenues generated by leases within the three mile zone. The segregated revenues shall be divided as otherwise provided by this Act except that the revenues attributable to such tract or tracts shall be first apportioned between the states on the basis of the portion of that tract which lies within three miles of the seaward boundary of each state.

Sec. 2. The Secretary shall distribute within sixty days of the effective date of this Act to each coastal State all funds deposited and held in a separate account in the Treasury of the United States under section 8(g)(4) of the Outer Continental Shelf Lands Act Amendments of 1978 (43 U.S.C. 1337(g)(4)) in a manner which provides that each coastal State for which reserves were deposited in such account shall receive 37 1/2 percent of the amount which should or would have been deposited in such account through the date of enactment of this Act under the terms of section 8(g)(2) and 8(g)(4) as herein provided. The Secretary shall also distribute, in accordance with the process established by section 8(g)(3) as herein provided, to each coastal State compensation for any drainage of State hydrocarbon resources by federal lessees through the date of enactment of this Act. The remaining balance of the funds in that account shall be deposited into the miscellaneous receipts account of the United States Treasury.

Sec. 3. Section 2(b) of the Submerged Lands Act. (43 U.S.C. 1301(b)) is amended by inserting before the semi-colon at the end of the subsection the following: ", except that any boundary between a State and the United States under this Act which has been or is hereafter fixed by coordinates under a final decree of the United States Supreme Court shall remain immobilized at the coordinates provided under such decree and shall not be ambulatory".

Sec. 4. Upon a final determination by a court of competent jurisdiction that the United States is entitled to any revenues which have been placed in escrow pursuant to section 7 of the Outer Continental Shelf Lands Act, the Secretary shall:

(a) distribute to the affected coastal State an amount equivalent to the State's entitlement under section 8(g)(2) as herein provided, and

(b) establish and deposit into a separate account in the Treasury of the United States an amount equivalent to 62 1/2 percent of royalties and accrued interest from lease tracts wholly or partially within three miles of the seaward boundary of such coastal State as established by the court decree, said royalties and interest to be held in the account until divided and distributed in accordance with section 8(g)(3) as herein provided.

BILL SHEFFIELD
GOVERNOR

State of Alaska
OFFICE OF THE GOVERNOR
WASHINGTON, D.C.

September 5, 1985

MEMORANDUM

TO: THE HONORABLE TED STEVENS, U.S. Senate
THE HONORABLE FRANK MURKOWSKI, U.S. Senate
THE HONORABLE DON YOUNG, U.S. House of Reps.
CURT MARSHALL, HARRY BURROUGHS, BUD DRAGO, Panama Canal/OCS Subcommittee, House Merchant Marine Committee
MARK TRAUTWEIN, Subcommittee on Energy and the Environment, House Interior and Insular Affairs Committee
RICHARD ARNOLD, JIM BRUCE, MIKE HARVEY, Senate Committee on Energy and Natural Resources

FROM: JOHN W. KATZ, Director of State/Federal Relations and Special Counsel to the Governor

MARTHA A. FOX, Special Assistant Attorney General

SUBJECT: 8(g) - LITIGATION FILED BY STATE

On September 3, 1985, the State of Alaska filed a complaint against the federal government under section 8(g) of the Outer Continental Shelf Lands Act (OCSLA). A copy is attached for your information.

The complaint seeks declaratory and injunctive relief from the court that would require the federal government to place into escrow all bonuses, royalties, and other revenues generated by the leasing of each tract wholly or partially within three miles of Alaska's seaward boundary. This request for relief is premised on several actions taken by the Interior Department. Interior has unilaterally adopted a practice of apportioning bonus revenues from each 8(g) tract in proportion to Interior's calculation of the percentage of that tract's surface acreage within three miles of Alaska's seaward boundary. Interior has also excluded from escrow all revenues from certain 8(g) tracts based upon its unilateral conclusion that these tracts lack hydrocarbon potential, despite the receipt of bonus bids

from oil companies. In the State's opinion, neither of these practices is supported by the 8(g) statute, which requires the deposit of all bonuses, royalties, and other revenues.

In addition to the escrow issues discussed above, the complaint requests declaratory relief entitling Alaska to access to all geological and geophysical data held by the federal government concerning the 8(g) zone, even if acquired outside the 8(g) zone. Further,the complaint seeks clarification that revenues from 8(g) tracts or potential 8(g) tracts in the Beaufort Sea must be deposited in the section 8(g) escrow account in the event that the United States prevails on the pending boundary litigation in United States v. Alaska which is currently before the United States Supreme Court.

Finally, the complaint seeks an order that provides for the fair and equitable division between the federal government and the State, of the revenues properly placed in the escrow account. In this regard, the State makes clear its claim that it is entitled to be compensated for drainage as well as receiving a fair and equitable share of the remaining royalty revenues.

Please call if you have any questions.

Attachment

cc: Rick Agnew
Greg Chapados
Tom Roberts
Tim Smith
Daryl H. Owen

HAROLD M. BROWN
ATTORNEY GENERAL
Mark P. Worcester
Assistant Attorney General
1031 W. 4th Avenue, Suite 200
Anchorage, Alaska 99501
(907)276-3550
Attorney for Plaintiff

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF ALASKA

STATE OF ALASKA,	)	
	)	
Plaintiff,	)	
	)	No.
vs.	)	
	)	
UNITED STATES OF AMERICA, UNITED STATES DEPARTMENT OF THE INTERIOR, DONALD PAUL HODEL, as Secretary of the Department of the Interior, UNITED STATES DEPARTMENT OF THE TREASURY, and JAMES A. BAKER, III, as Secretary of the Department of the Treasury.	)	
	)	
Defendants.	)	
	)	

COMPLAINT

1. This is a civil action pursuant to Public Law 95-372, the Outer Continental Shelf Lands Act Amendments of 1978 (the "1978 Amendments"), which amended the Outer Continental Shelf Lands Act ("OCSLA"), 43 U.S.C. 1311, et seq. Generally, and as

more fully set forth below, this suit seeks an order effecting the fair and equitable division between the United States of America and the State of Alaska of revenues generated as a result of certain oil and gas leasing in the federal Outer Continental Shelf ("OCS"). It also seeks declaratory and injunctive relief requiring the proper escrow of these revenues pending their division, either by agreement or order of this court, and the enforcement of Alaska's right of access to certain data, all as required by 43 U.S.C. 1337(g) (section "8(g)").

JURISDICTION

2. This court has jurisdiction pursuant to 5 U.S.C. 702 (review of agency action), 28 U.S.C. 1331(a) (federal question), 28 U.S.C. 2201 and 2202 (declaratory judgment), and 43 U.S.C. 1337(g)(4). All preconditions to suit have been met.

VENUE

3. Venue is proper in this court under 28 U.S.C. 1391.

PARTIES

4. Plaintiff State of Alaska ("Alaska") is a sovereign state of the United States of America, having been admitted to the Union on January 3, 1959 pursuant to the Alaska Statehood Act, Public Law 85-508, 72 Stat. 339 (1958). Alaska appears on its own right, and on behalf of its agencies, employees and citizens.

5. Defendant United States of America ("United States") is the government of the federal union comprised of the fifty United States, of which Alaska is one.

6. Defendant United States Department of the Interior ("Interior") is a department of the executive branch of the United States, and is primarily responsible for compliance with the requirements of section 8(g), including the requirement of proper deposits into those separate accounts which were or should have been established pursuant to section 8(g) ("8(g) escrow accounts").

7. Defendant Donald Paul Hodel is Secretary of the Interior ("Secretary"), and in such capacity is charged with ensuring Interior's compliance with section 8(g).

8. Defendant United States Department of the Treasury ("Treasury") is a department of the executive branch of the United States, and is responsible for maintaining 8(g) escrow accounts in accordance with section 8(g).

9. Defendant James A. Baker, III is Secretary of the Treasury and in such capacity is charged with responsibility for ensuring Treasury's compliance with its 8(g) escrow account obligations.

GENERAL ALLEGATIONS

10. The OCSLA, as amended, imposes certain obligations and requirements upon the defendants relating to the leasing for oil

and gas exploration purposes of the OCS land located within three miles of the seaward boundary of Alaska (the "8(g) zone").

11. Under 43 U.S.C. 1337(g)(1) the Secretary must provide to Alaska certain information, including "all information concerning the geographical, geological, and ecological characteristics" of the 8(g) zone.

12. Under 43 U.S.C. 1337(g)(2) the Secretary must offer the Governor of Alaska the opportunity to enter into an agreement concerning the fair and equitable disposition of revenues which may be generated from the leasing of tracts wholly or partially within the 8(g) zone ("8(g) tracts").

13. Under 43 U.S.C. 1337(g)(4), the Secretary must, in the absence of an agreement disposing of revenues generated by the leasing of 8(g) tracts, deposit into a separate account in the Treasury "all bonuses, royalties, and other revenues" generated by the leasing of 8(g) tracts.

14. Treasury and its Secretary must maintain the revenues deposited into 8(g) accounts, together with accrued interest, until their disposition is effected by agreement between the Governor of Alaska and the Secretary of the Department of the Interior or by order of this court.

15. Under 43 U.S.C. 1337(g)(4), in the absence of agreement between the Governor of Alaska and the Secretary, this court must divide all bonuses, royalties, and other revenues

generated by the leasing of 8(g) tracts on a fair and equitable basis.

COUNT I

FAIR AND EQUITABLE DIVISION

16. Since the effective date of the Act, the defendants have held the following oil and gas lease sales involving 8(g) tracts adjacent to Alaskan waters: the Joint Federal-State Beaufort Sea Sale (the "Beaufort Sea Sale") (December 1979); Sale 60 (September 1981); Sale 71 (October 1982); and Sale 87 (August 1984).

17. The Beaufort Sea Sale, Sale 60, Sale 71 and Sale 87 have generated substantial revenues.

18. No valid agreement for the fair and equitable division of bonuses, royalties, and other revenues generated by defendants' leasing of 8(g) tracts has been executed between the Governor of Alaska and the Secretary for 8(g) tracts leased in the Beaufort Sea Sale, Sale 60, Sale 71 or Sale 87.

19. Fairness and equity require the court to award to Alaska complete compensation for drainage, i.e., all royalties attributable to oil and gas originally in place underneath state land, but produced from wells on tracts in the 8(g) zone.

20. Fairness and equity require that in addition compensation for drainage, the court award to Alaska half of the 8(g) bonuses, royalties and other revenues except as special equitable circumstances, determined under the totality of the

circumstances, justify a deviation from an even sharing between Alaska and the United States.

21. Special circumstances which must be considered in making this fair and equitable division, and which require a greater distribution of 8(g) revenues to Alaska, include, without limitation, the following:

(a) a consideration of the extent to which federal revenues, including oil and gas lease bonuses for 8(g) tracts, are enhanced on account of geological, geophysical and other information generated either under Alaska permits or on account of Alaska's oil and gas leasing activities;

(b) a consideration of the extent to which federal revenues, including oil and gas lease bonuses for 8(g) tracts, are enhanced and made possible by the infrastructure, including the Trans-Alaska Pipeline ("TAPS"), other pipelines, and storage and production facilities, developed as a result of Alaska's oil and gas leasing and other activity;

(c) a consideration of the extent to which federal revenues, including oil and gas lease bonuses for 8(g) tracts, are enhanced by advances in oil industry technology developed as a result of Alaska's oil and gas leasing activity;

(d) a consideration of the extent to which defendants have failed to realize fair market value from the oil and gas leasing of 8(g) tracts through their use of an area wide leasing

system, their selection of bidding systems, and other aspects of their oil and gas leasing policies;

(e) a consideration of the costs, burdens and risks of federal OCS oil and gas leasing, including the leasing of 8(g) tracts, upon Alaska and its people; and

(f) a consideration of the statutory purpose of providing the states with incentives for cooperating in OCS oil and gas development, and of Alaska's cooperation in that development.

22. Alaska is entitled to a fair and equitable share of bonuses, royalties and other revenues, with interest, attributable to the leasing of any tract wholly or partially within three miles of Alaska's seaward boundary, with provisions for adjustments according to wherever that boundary may ultimately be determined to lie.

COUNT II

ESCROW ACCOUNTS

23. Defendants have failed to comply with their common law trust and statutory obligations to establish, account for, maintain and provide notice concerning proper 8(g) accounts in order to protect Alaska's rights and interests in all bonuses, royalties, interest and other revenues generated by defendant's leasing of 8(g) tracts.

24. No separate 8(g) escrow account has been established for the Beaufort Sea Sale.

25. Revenues from lease tracts whose ownership is disputed, but which would be 8(g) tracts if the United States were to prevail in pending boundary litigation in United States v. Alaska, Supreme Court No. 84, Original, are held in a separate account of the Treasury pursuant to section 7 of the OCSLA, 43 U.S.C. 1336. To the extent some or all of these tracts would be 8(g) tracts based upon the ultimate determination in the boundary litigation, revenues attributable to those tracts, with interest, should be deposited in 8(g) escrow accounts at the time of that ultimate boundary determination.

26. Revenues from at least four 8(g) tracts in the Beaufort Sea Sale, designated as (Block Number/Lease Number) 471/BF-2, 472/BF-3, 473/BF-4 and 474/BF-5A, have not been put into any escrow account, whether labeled by defendants as a "section 7" or a "section 8(g)" escrow account.

27. Defendants have improperly made changes in the escrow accounts for revenues attributable to 8(g) tracts adjacent to Alaska without notice to, consultation with, or consent of, Alaska.

28. By unilaterally adopting a practice of apportioning bonus revenues from each 8(g) tract in proportion to defendants' calculation of the percentage of that tract's surface acreage within three miles of Alaska's seaward boundary, defendants have improperly omitted from their 8(g) escrow deposits approximately

two thirds of the amount which should be in escrow for Alaska. This practice has resulted in an estimated deficiency in excess of $420 million in the 8(g) escrow accounts for Alaska.

29. In a practice instituted in Alaska for Sale 87, defendants improperly began to exclude from escrow all revenues from some 8(g) tracts based upon defendants unilateral conclusion that such tracts lacked hydrocarbon potential, even though bids based upon a contrary assessment were made by oil companies and accepted by defendants. Bonus bids of approximately $142 million for 8(g) tracts in Sale 87 were entirely omitted from escrow under this practice.

30. Alaska is entitled to a declaration that defendants have improperly executed their escrow obligations under 43 U.S.C. 1337(g)(4), and to an order requiring defendants to deposit into escrow in a separate account of the Treasury an amount equal to the sum of all bonuses, royalties, and other revenues, with interest, generated by the leasing of each tract wholly or partially within three miles of Alaska's seaward boundary, with provisions for adjustments according to wherever that boundary may ultimately be determined to lie, pending the disposition of such revenues pursuant to agreement between the Secretary and the Governor or Alaska or by court order.

COUNT III

INFORMATION SHARING

31. Defendants have violated 43 U.S.C. 1337(g)(1) by failing to provide to Alaska all geological and geophysical information required under that provision.

32. From the time of the passage of the 1978 Amendments until approximately February 1985, defendants violated 43 U.S.C. 1337(g)(1) by refusing to provide any geological and geophysical data other than those data acquired from areas which defendants unilaterally judged were overlying common geological structures.

33. Commencing in approximately February 1985, defendants began providing Alaska with geological and geophysical data acquired anywhere within the 8(g) zone, but improperly continue to refuse to provide to Alaska data collected outside the 8(g) zone, even though those data concern the geological and geophysical characteristics of the 8(g) zone.

34. Alaska is entitled to a declaratory judgment and an injunction providing Alaska with access to all geological and geophysical data held by defendants concerning the 8(g) zone, even if acquired outside the 8(g) zone.

PRAYER

Alaska prays that the court:

1. Declare defendants have not complied with their information sharing obligations under 43 U.S.C. 1337(g), and

order compliance with that section with regard to past and future oil and gas sales involving 8(g) tracts;

2. Declare that, by prorating bonuses on a surface acreage basis, by excluding all revenues from some 8(g) tracts based upon defendants' unilateral conclusions that those tracts lack hydrocarbon potential, and by other practices, defendants have improperly executed their escrow obligations under 43 U.S.C. 1337(g)(4);

3. Order defendants to deposit into escrow in a separate account of the Treasury of the United States an amount equal to the sum of all bonuses, royalties, and other revenues generated by the leasing of each tract wholly or partially within three miles of Alaska's seaward boundary, with provisions for adjustments according to wherever that boundary may ultimately be determined to lie, pending the disposition of such revenues pursuant to agreement between the Secretary and the Governor or Alaska or by court order;

4. Determine and order the fair and equitable disposition between Alaska and the United States of all bonuses, royalties and other revenues, with interest, generated by the leasing of all tracts wholly or partially within three miles of Alaska's seaward boundary, with provisions for adjustments according to wherever that boundary may ultimately be determined to lie;

5. Grant Alaska's costs of suit; and

6. Grant such other and further relief to Alaska as the court may find to be just and proper.

DATED this 3rd day of September, 1985.

HAROLD M. BROWN
ATTORNEY GENERAL
STATE OF ALASKA

By: _____
Mark P. Worcester
Assistant Attorney General

GEORGE DEUKMEJIAN
GOVERNOR

State of California
GOVERNOR'S OFFICE
SACRAMENTO 95814

TELEPHONE
(916) 445-2841

September 23, 1985

Honorable James A. McClure
Chairman, Committee on
Energy and Natural Resources
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

I am writing to inform you of my views on proposed legislation concerning the sharing of funds prescribed by section 8(g) of the Outer Continental Shelf (OCS) Lands Act. As you are aware, in approving the budget Congress directed that legislation be enacted to provide for disposition of OCS revenues currently being held in a separate escrow account in the Treasury. Congress' direction was to give affected states a 27 percent share of bonuses, rents and accrued interest in this account.

As I wrote to you in July, I feel strongly that legislation concerning the division of future 8(g) revenues should include sharing of royalties paid to the federal government. At present, few of the 8(g) tracts covered by the escrow account are producing royalties. However, this source of 8(g) revenues will become increasingly important over the next twenty years and beyond if energy development continues at its present pace offshore California. This state and the affected local governments urgently need this source of 8(g) revenues if we are to be able to accommodate this development.

In addition, I do not see the sharing of royalties as simply a drainage issue. Limiting royalties to payment for drainage from beneath state tidelands is neither fair nor equitable. This approach merely reimburses the state for resources which are already ours.

I would appreciate your help in ensuring that a provision for sharing royalties is incorporated into the legislation regarding future 8(g) revenue distributions. Should you have any specific questions, please contact my Secretary of Environmental Affairs and OCS Policy Coordinator, Jananne Sharpless at (916) 322-5846.

Most cordially,

George Deukmejian

George Deukmejian

eh